No. 00-568-CFX Title: New York, et al., Petitioners
v.
Federal Energy Regulatory Commission, et al.

Docketed: October 13, 2000 Court: United States Court of Appeals for the District of Columbia Circuit

Vide:
00-809

Entry	Date	Proceedings and Orders
	Oct 12 2000	Petition for writ of certiorari filed. (Response due January 26, 2001)
	Oct 12 2000	Volume two of petition filed.
	Oct 30 2000	Waiver of right of respondent Consumers Energy Company to respond filed.
	Oct 30 2000	Waiver of right of respondent National Rural Electric Cooperative Assn. to respond filed.
	Oct 30 2000	Waiver of right of respondent Indianapolis Power & Light Co. to respond filed.
	Nov 3 2000	Waiver of right of respondent Puget Sound Energy, Inc. to respond filed.
	Nov 3 2000	Order extending time to file response to petition until December 13, 2000.
	Nov 3 2000	This extension is granted for all respondents.
	Nov 7 2000	Waiver of right of respondent Commonwealth Edison Company to respond filed.
	Nov 8 2000	Waiver of right of respondent Citizens Action Coalition of Indiana, Inc. to respond filed.
	Nov 9 2000	Waiver of right of respondent IN Industrial Energy Consumers, Inc. to respond filed.
	Nov 13 2000	Waiver of right of respondent Dairyland Power Coop. to respond filed.
	Dec 6 2000	Order further extending time to file response to petition until January 26, 2001.
	Dec 6 2000	This extension of time is granted to all respondents.
	Jan 16 2001	Waiver of right of respondents New York State Electric & Gas Corporation, et al. to respond filed.
	Jan 26 2001	Brief of respondent Transmission Access Policy Study Group in opposition filed. VIDED.
	Jan 26 2001	Brief of respondent Federal Energy Regulatory Commission in opposition filed. VIDED.
	Jan 29 2001	Waiver of right of respondent Transmission Dependent Utility Systems to respond filed.
	Feb 2 2001	Reply brief of petitioners New York, et al. filed.
	Feb 7 2001	DISTRIBUTED for Conference of February 23, 2001
	Feb 21 2001	Waiver of right of respondent Municipal Electric Utilities of Wisconsin to respond filed.
	Feb 26 2001	Petition GRANTED. limited to Question 1 presented by the petition. The case is consolidated with No. 00-809, Enron Marketing, Inc., v. FERC, and a total of one hour is allotted for oral argument. SET FOR ARGUMENT October 3, 2001.

****

3pp

No. 00-568-CFX

Entry	Date	Proceedings and Orders
	Mar 27 2001	Order extending time to file the briefs on the merits. The briefs on the merits for New York, et al. and Enron, as petitioners, are to be filed on or before April 19, 2001, with any amicus curiae briefs supporting petitioners to be filed on the same day. The briefs on the merits of New York, et al. and Enron, as respondents, are to be filed on or before May 10, 2001. The briefs on the merits of respondents FERC, et al., are to be filed on or before May 31, 2001, with any amicus curiae briefs supporting respondents to be filed on the same day. Replybriefs, if any, are to be filed on or before July 2, 2001.
	Mar 30 2001	The Clerk has approved the use of the deferred joint appendix.
	Apr 19 2001	Brief of petitioner Enron Power Marketing, Inc. filed. VIDED.
	Apr 19 2001	Brief of respondent Electric Power Supply Association in support of petition filed. VIDED.
	Apr 19 2001	Brief of respondents Electricity Consumers Resource Council, et al. in support of petition filed. VIDED.
	Apr 19 2001	Brief of petitioners Public Service Commission of State of New York, et al. filed.
	Apr 19 2001	Brief amici curiae of California and Public Utilities Commission of California filed.
	May 10 2001	Brief of respondent Enron Power Marketing, Inc. filed. VIDED.
	May 10 2001	Brief of respondents Public Service Commission of State of New York, et al. filed. VIDED.
	May 31 2001	Motion of Pennsylvania Public Utility Commission for leave to file a brief as amicus curiae filed.
	May 31 2001	Brief of respondent Transmission Access Policy Study Group filed.
	May 31 2001	Brief of respondent Edison Electric Institute filed. VIDED.
	May 31 2001	Brief amici curiae of Electrical Engineers, Energy Economists and Physicists filed. VIDED.
	May 31 2001	Brief of respondent Federal Energy Regulatory Commission filed. VIDED.
	Jun 7 2001	Application (00A1091) of State PUC's, et al., for leave to file a reply brief in excess of the page limitation, submitted to The Chief Justice.
	Jun 13 2001	Application (00A1091) denied by the Chief Justice.
	Jun 14 2001	Order extending time to file the joint appendix to and including June 18, 2001.
	Jun 15 2001	Motion of the Solicitor General for additional time for oral argument and for divided argument filed.
	Jun 18 2001	Joint appendix filed. VIDED.
	Jun 18 2001	* Jt. appendix filed in two volumes.
	Jun 29 2001	Motion of Pennsylvania Public Utility Commission for leave to file a brief as amicus curiae GRANTED.
	Jun 29 2001	Motion of the Solicitor General for additional time for oral argument and for divided argument GRANTED. and ten additional minutes are allotted for oral argument to be divided as follows: 20 minutes for petitioners in No. 00-568, 20 minutes for petitioner in No. 00-809, and 30 minutes for the Solicitor General. The request for divided rebuttal is denied.
	Jul 2 2001	Reply brief of petitioner Enron Power Marketing, Inc. filed. VIDED.
	Jul 2 2001	Reply brief of petitioners Public Service Commission of the State of New York filed. VIDED.
	Jul 2 2001	Reply brief of respondent Citizens Action Coalition of Indiana, Inc. filed.
	Jul 20 2001	CIRCULATED.
	Sep 6 2001	LODGING consisting of twenty copies of material from Introduction to Electrical Theory and Power Transmission by Robert Sarikas submitted by amicus Electrical Engineers et al., and distributed.
	Sep 12 2001	Record filed.
	Oct 3 2001	ARGUED.

Supreme Court, U.S.
FILED
00 568 OCT 12 2000
OFFICE OF THE CLERK

No.

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK and THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioners,

-v-

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

PETITION FOR A WRIT OF CERTIORARI
Volume I

LAWRENCE G. MALONE*
General Counsel
JONATHAN D. FEINBERG
DIANE T. DEAN
Assistant Counsel
NYS-Dept. of Public Service
Public Service Commission
3 Empire State Plaza
Albany, NY 12223-1350
(518) 474-2510

**Counsel of Record*

October 11, 2000

(Additional Counsel on Inside Cover)

425 pp

CHARLES D. GRAY
National Association of
Regulatory Utility Commissioners
1100 Pennsylvania Avenue, N.W.
Suite 603, P.O. Box 684
Washington, D.C. 20044-0684
(202) 898-2208

CATHERINE BEDELL
General Counsel
RICHARD BELLAK
Associate General Counsel
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Fl 32399-0850
(850) 413-6092

ALAN G. LANCE
Attorney General
DONALD L. HOWELL, II
Deputy Attorney General
Idaho Public Utilities Commission
472 West Washington Street
P.O. Box 83720
Boise, ID 83720-0074
(208) 334-0312

JOHN J. FARMER, JR.
Attorney General
State of New Jersey
By: HELENE S. WALLENSTEIN
Sr. Deputy Attorney General
Attorney for New Jersey Board
of Public Utilities
124 Halsey Street 5th Floor
P.O. Box 45029
Newark, NJ 07101
(973) 648-4846

JOANNE SANFORD
North Carolina Utilities
Commission
ROBERT P. GRUHER
Public Staff, North Carolina
Utilities Commission
GISELE L.RANKIN
Staff Attorney
P.O. BOX 29520
RALEIGH, NC 27626-0520
(919) 733-2435

WILLIAM H. CHAMBLISS
General Counsel
C. MEADE BROWDER, JR.
Attorney Virginia State
Corporation Commission
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218
(804) 371-9671

CHRISTINE O. GREGOIRE
Attorney General
WILLIAM BERGGREN COLLINS
Senior Assistant Attorney General
ROBERT D. CEDARBAUM
Senior Counsel for the Washington
Utilities and Transportation Commission
P.O. Box 40128
Olympia,WA 98504-0128
(360) 664-1188

HARVEY L. REITER
for the Vermont Department of
Public Serice
MORRISON & HECKER
1150 18th Street, N.W., Suite 800
Washington, D.C. 20036
(202) 785-9100

HARRY IVEY
for the Wyoming Public Service
Commission
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002
(307) 777-7824

THE REPORTER COMPANY, *Printers and Publishers, Inc.*
181 Delaware Street, Walton, NY 13856—800-252-7181
(2817 – 2000)

Printed on Recycled Paper

QUESTIONS PRESENTED

1. Whether, given that Congress in 1935 stated that federal regulation extends "only to those matters which are not subject to regulation by the states" (Federal Power Act (FPA) § 201(a)), and the transmission of energy from generators to retail customers in the same state was then "subject to regulation by the states" (as it has been since 1935), may the Federal Energy Regulatory Commission (FERC) preempt state jurisdiction over such intrastate retail transmissions of electric energy?

2. Whether, given that FPA § 201(b) expressly denies FERC jurisdiction over local distribution facilities, may FERC preempt state jurisdiction over local distribution facilities when they are used for wholesale sales?

3. Whether FERC can assert jurisdiction over costs utilities incur to provide retail services when those costs become unrecoverable as a result of competition?

4. Should the Court, in resolving questions 1-3, defer to FERC's reading of its own jurisdictional limitations?

PARTIES

Petitioners are the Public Service Commissions of Florida, New York and Wyoming, the Public Utilities Commissions of Idaho and North Carolina, the New Jersey Board of Public Utilities, the Vermont Board of Public Utilities, the Virginia State Corporation Commission, the Washington Utilities and Transportation Commission, and the National Association of Regulatory Utility Commissioners. Pursuant to Rule 29.6 of this Court's Rules, none of the Petitioners/Intervenors State Utility Commissions, which are governmental agencies, needs to file a corporate disclosure statement.

The National Association of Regulatory Utility Commissioners (NARUC) is a quasi-governmental non-profit corporation organized under the laws of the District of Columbia. The NARUC has no corporate parents or affiliates that have issued shares or debt securities to the public. Within its membership are the governmental bodies of the fifty States engaged in the economic and safety regulation of carriers and utilities. The remaining parties to the underlying proceeding are listed in Petitioners' Appendix, "Pet. App." R.

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED i

PARTIES ii

TABLE OF AUTHORITIES vi

INDEX TO APPENDICES x

OPINIONS BELOW 1

JURISDICTION 1

STATUTORY PROVISIONS INVOLVED 2

STATEMENT OF THE CASE 2

A. Enactment Of The Federal Power Act 2

B. FERC's Decision Under Review 5

C. The D.C. Circuit's Decision 7

REASONS FOR GRANTING THE WRIT 8

ARGUMENT 10

Page

POINT I 10

THE DECISION ALLOWING FERC TO PREEMPT THE STATES' REGULATION OF THE TRANSMISSION OF ELECTRICITY FROM A GENERATOR TO A RETAIL CUSTOMER IN THE SAME STATE CONFLICTS WITH THIS COURT'S TEACHING IN HILLSBOROUGH, IMPERMISSIBLY DEFERS TO FERC'S READING OF THE STATUTE LIMITING THAT AGENCY'S JURISDICTION AND CONFLICTS WITH CONGRESS' RESERVATION OF STATE JURISDICTION OVER INTRASTATE TRANSMISSIONS OF ELECTRICITY 10

POINT II 19

THE DECISION THAT FERC MAY PREEMPT STATE REGULATION OF UTILITIES' LOCAL DISTRIBUTION SYSTEMS WHEN ENERGY IS RESOLD CONFLICTS WITH CONGRESS' DIRECTION THAT LOCAL DISTRIBUTION OF ELECTRICITY BE REGULATED BY THE STATES 19

Page

POINT III 22

THE HOLDING THAT FERC MAY PREEMPT STATE AUTHORITY OVER UTILITY COSTS INCURRED UNDER STATE SUPERVISION TO SERVE RETAIL CUSTOMERS VIOLATES CONGRESS' RESERVATION OF RETAIL ELECTRIC RATE JURISDICTION TO THE STATES 22

CONCLUSION 25

TABLE OF AUTHORITIES

Cases: **Page**

American Textile Mfrs. Inst. v. Donovan, 452 U.S. 490 (1981) 15

Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375 (1983) 9, 17

California v. ARC America Corp., 490 U.S. 93 (1989) 18, 19

Chemehuevi Tribe of Indians v. Federal Power Comm'n, 420 U.S. 395 (1975) 17

Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) 9, 11

Connecticut Light & Power v. Federal Power Comm'n, 324 U.S. 515 (1945) 19, 20

Duke Power Co. v. Federal Power Comm'n, 401 F.2d 930 (D.C. Cir. 1968) 20

Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989) 23

Federal Power Comm'n v. Florida Power & Light Co. (FP&L), 404 U.S. 453 (1972) . . . . . *passim*

Fidelity Federal Savings and Loan Ass'n v. De la Cuesta, 458 U.S. 141 (1982) 7

Page

Food and Drug Administration v. Brown and Williamson Tobacco Corp., __ U.S. __, 120 S. Ct. 1291 (2000) 15

Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205 (1964) . . . . . *passim*

Henry v. Federal Power Comm'n, 513 F.2d 395 (D.C. Cir. 1975) 17

Hillsborough County, Florida v. Automated Medical Labs, Inc., 471 U.S. 707 (1985) . . . . . *passim*

Iowa Utilities Board v. Federal Communications Comm'n, 219 F.3d 744 (8th Cir. 2000) 15

Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61 (1943) . . . . . *passim*

Jones v. Rath Packing Co., 430 U.S. 519 (1977) 8, 10

Louisiana Pub. Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355 (1986) 22, 25

Medtronic, Inc. v. Lohr, 518 U.S. 484 (1996) 19

Mississippi Industries v. Federal Energy Regulatory Commission, 808 F.2d 1525 (D.C. Cir. 1987) 23

Nantahala Power and Light Co. v. Thornburg, 476 U.S. 953 (1986) 22

Page

Northern States Power Co. v. Federal Energy Regulatory Comm'n, 176 F.3d 1090 (8th Cir. 1999), rehearing denied, 1999 U.S. App. LEXIS 23493 (8th Cir. 1999), cert. denied, 120 S. Ct. 1221, __ U.S. __ (2000) 17

Oklahoma Natural Gas Co. v. FERC,, 28 F.3d 1281 (D.C. Cir. 1994) 11

Public Utilities Comm'n of Rhode Island v. Attleboro Steam and Electric Co., 273 U.S. 83 (1927) ..... *passim*

Rice v. Santa Fe Elevator Corp., 331 U.S. 218 (1947) 10

Schreiber v. Burlington Northern, Inc., 472 U.S. 1 (1985) 15

United States v. Bass, 404 U.S. 336 (1971) 11

Wisconsin-Michigan Power Co. v. Federal Power Comm'n, 197 F.2d 472 (7th Cir. 1952) 20

Page

Statutes:

Federal Power Act:
§ 201(a) ..... *passim*
§ 201(b) ..... *passim*
§ 201(b)(1) 3, 8, 19
§ 201(c) ..... *passim*
§ 202 14
§ 203 14
§ 204 14
§ 205 ..... 14, 15, 17
§ 212(h) 3, 15, 16, 17

16 U.S.C.:
§ 824(a), (b) and (c) 3
§ 824(b)(1) 3, 8

28 U.S.C. § 1254(1) 2

INDEX TO APPENDICES

Page

Appendix A - Order of United States Court of Appeals for the District of Columbia Circuit filed August 22, 2000 ..... A-1

Appendix B - Judgment of United States Court of Appeals for the District of Columbia Circuit filed June 30, 2000 ..... B-1

Appendix C - Opinion of United States Court of Appeals for the District of Columbia Circuit decided June 30, 2000 ..... C-1

Appendix D - Section 31,036 Federal Energy Regulatory Commission Regulations Preambles (Order 888) D-1

Appendix E - Section 31,048 Federal Energy Regulatory Commission Regulations Preambles (Order 888-A) E-1

Appendix F - 81 FERC Section 61,248 (Order 888-B) F-1

Appendix G - Statutory Provisions Involved G-1

Appendix H - H. Rep., Hearings Before the Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce, 90th Cong., 1st Sess. (1967), excerpts from Testimony of FPC Chairman Lee C. White H-1

Page

Appendix I - H. Rep., Hearings Before the Subcommittee on Interstate and Foreign Commerce, 74th Cong., 1st Sess. (1935) Frank R. McNinch, Chairman, Federal Power Commission, introducing Testimony of FPC Commissioner Clyde L. Seavey and excerpts from Seavey Testimony I-1

Appendix J - New York Times, June 8, 1935, "Utility Foes Map Floor Fight" J-1

Appendix K - Hearings before the Committee on Interstate and Foreign Commerce House of Representatives 74th Congress, 1st Session, (1935), excerpts from Testimony of John E. Benton, General Solicitor, NARUC K-1

Appendix L - Hearings before the Committee on Interstate and Foreign Commerce House of Representatives, 74th Congress, 1st Session, (1935), excerpts from Testimony of Dozier DeVane, Solicitor, Federal Power Commission L-1

Appendix M - Hearings before a Subcommittee of the Committee on Interstate and Foreign Commerce House of Representatives, 80th Congress, 1st Session (1947), excerpts from Testimony of Howard E. Wahrenbrock, Assistant General Counsel, Federal Power Commission M-1

Page

Appendix N - Hearings before the Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce House of Representatives, 80th Congress, 1st Session (1947), excerpts from Testimony of Nelson Lee Smith, Chairman, Federal Power Commission N-1

Appendix O - Excerpts from Supreme Court Brief of Federal Power Commission in *Federal Power Commission v. Florida Power & Light Company* O-1

Appendix P - Senate Report No. 621, 74th Congress 1st Session and House Report No. 1318, 74th Congress 1st Session (1935) P-1

Appendix Q - Glossary of Terms Q-1

Appendix R - List of Parties R-1

PETITION FOR A WRIT OF CERTIORARI

Petitioners/Intervenors State Public Service Commissions, which regulate retail electric rates and service for some 63 million people, and the National Association of Regulatory Utility Commissioners (State Commissions et al.), petition for a writ of certiorari to review a judgment of the United States Court of Appeals for the D.C. Circuit that allowed the Federal Energy Regulatory Commission (FERC) to (1) preempt state regulation of the transmission of electricity from generators to retail customers in the same state, (2) preempt state regulation of local systems used to deliver electricity when the electricity is resold, and (3) set transmission rates that recover a utility's generation costs "stranded" due to municipalization or retail competition.[1/]

OPINIONS BELOW

The Opinion of the District of Columbia Circuit, Pet. App. C, is at _ F.3d _, 2000 U.S. App. Lexis 15362. The Court's order on rehearing (Pet. App.A) is not officially reported. FERC Order 888 is reported at FERC Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540. FERC's rehearing decisions (Orders 888-A and 888-B) are reported respectively at FERC Stats. & Regs. ¶ 31,048 and 81 FERC ¶ 61,248 (1997). Pertinent portions of the FERC orders are supplied in Pet. App. D, E, and F.

JURISDICTION

The judgment of the Court of Appeals was entered June 30, 2000. The order denying rehearing was issued August 22, 2000. The Petition for Certiorari is timely because it was filed within 90 days from the date of denial of the Petition for Rehearing

---

1/ "Municipalization," "retail transmission," "wholesale sales" and other relevant terms are defined in the Glossary of Terms contained in the Appendices, Pet. App. Q.

en banc. Supreme Court Rule 13(3). The Petition for Rehearing en banc was filed within 45 days of the D.C. Circuit's judgment, as required by D.C. Circuit Rule 35. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The relevant statutory provisions are provided in Pet. App. G.

STATEMENT OF THE CASE

A. Enactment Of The Federal Power Act

Electric service involves the generation of electricity and either (i) its transmission and local distribution to the ultimate consumer (a retail sale) or (ii) its transmission to a reseller (a wholesale sale) who transmits and distributes the power to an end user (a retail sale). State commissions have traditionally regulated all aspects of bundled retail transactions, including service issues and the intrastate sale and distribution of electricity.

Traditionally, FERC has regulated wholesale power sales and interstate transmission of electricity, which represent a small percentage of the total revenues from use of electric systems. See H. Rep., Hearings Before The Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce, 90th Cong., 1st Sess. (1967), 1967 Hearings, Testimony of FPC Chairman Lee C. White at 124. Pet App. H-14. In particular, when Congress enacted the 1935 Federal Power Act (FPA), the states were regulating the rates that utilities charged to deliver electricity from a generator to a retail consumer in the same state. H. Rep., Hearings Before the Subcommittee on Interstate and Foreign Commerce, 74th Cong.,

1st Sess. (1935) "1935 Hearings," Testimony of FPC Commissioner Clyde L. Seavey, at 420. Pet. App. I-4.

Congress passed the FPA not to override state regulation -- indeed it insisted state regulation was not to be affected -- but to fill a jurisdictional gap created by a Supreme Court decision that states could not set rates for wholesale energy sold across state lines. Public Utilities Comm'n of Rhode Island v. Attleboro Steam and Electric Co., 273 U.S. 83, 89 (1927). Congress filled this "Attleboro Gap" by empowering the Federal Power Commission (FPC) to regulate wholesale electricity rates because, in the absence of federal regulation, there would be no regulation of interstate sales. Hence, § 201(a) provides that federal regulation is "however, to extend only to those matters which are not subject to regulation by the States" (emphasis added).

In closing the "Attleboro Gap," Congress preserved the states' jurisdiction over the intrastate retail transmission of electricity. In fact, the FPA expressly safeguarded state regulation of all retail sales and local distribution systems. FPA § 201(b). While Congress empowered the FPC to regulate wholesale sales of electricity in interstate commerce, it expressly provided that the FPC, now Federal Energy Regulatory Commission (FERC), was not to regulate (a) any aspect of the delivery of electricity from a generator to a retail consumer in the same state,[2/] or (b) the use of local distribution facilities.[3/] This Court has emphasized that the specific language of FPA section 201(b) expressed Congress' intent to draw a "bright line" easily ascertainable between state and federal jurisdiction:

[2/] FPA § 201(a), (b)(1), (c) [16 U.S.C. § 824(a), (b) and (c)]; § 212(h) [16 U.S.C. § 824k(h)].

[3/] FPA § 201(b)(1) [16 U.S.C. § 824(b)(1)].

> What Congress did was to adopt the test developed in the Attleboro line which denied state power to regulate a sale 'at wholesale to local distributing companies' and allowed state regulation of a sale 'at local retail rates to ultimate consumers.' [citation omitted].

Federal Power Commission v. Southern California Edison Co., 376 U.S. 205, 214 (1964).

The FPA's legislative history is consistent with its express language preserving state jurisdiction. In 1935, most electric facilities were intrastate facilities. 1935 Hearings, at 420. Pet. App. I-12. House Rep. No. 1318, 74th Cong., 1st Sess. (1935) at 7. Pet. App. P-22. Thus, states' rights advocates in Congress added the "intrastate" clause to the FPA "so that [the Act] specifically will not apply to intrastate business." New York Times, June 8, 1935, "Utility Foes Map Floor Fight;" see 1935 Hearings, Testimony of John E. Benton, General Solicitor, NARUC, at 760, 763 et seq; see also Senate Rep. No. 621, 74th Cong., 1st Sess. (1935) at 18. Pet. App. J-1; K-5 and P-4.

FERC's predecessor, the Federal Power Commission (FPC), repeatedly conceded that the purposes of the FPA were limited to filling the "Attleboro gap" and protecting state jurisdiction. Dozier DeVane, Solicitor of the FPC, stated to the House Committee on Interstate and Foreign Commerce that:

> ... [S]ection 201 is intended to give the Federal Power Commission jurisdiction over the wholesale rates only. (1935 Hearings at 497) ... [T]he plan of this bill with reference to the regulation of rates [is that] it seeks to leave in the state commissions the power to regulate retail rates but through some federal agency assist the state commissions making

> available to them the proper data for the determination of those rates.

1935 Hearings, at 520. Pet. App. L-14. Further, the FPC acknowledged to Congress in 1947 that its jurisdiction did not include "the regulation of rates and service outside of [the Attleboro Gap]." A Bill to Amend Section 201 of the Federal Power Act, Hearings Before Subcommittee on Interstate and Foreign Commerce, 80th Cong., 1st Sess., (hereinafter "1947 Hearings"), at 506. Pet. App. M-1. The FPC stated "The bill provides that the [FPC] may regulate the rates that no State commission can regulate. The bill simply fills this gap and that is all." 1935 Hearings at 549. Pet. App. L-34.

B. FERC's Decision Under Review

Notwithstanding the FPA's clear reservation of state authority over retail and intrastate matters, in 1998 FERC preempted state regulation of both the delivery of electricity from a generator to a retail consumer in the same state and the use of local distribution facilities to deliver electricity that is resold. FERC envisioned the introduction of competition, not only in its jurisdictional market (wholesale sales) but also in the state jurisdictional retail market and concluded that competition allowed it to expand its jurisdiction in three areas.

First, FERC asserted jurisdiction over retail transactions when states unbundled retail rates into charges for delivery and electricity.[4/] Specifically, FERC reasoned that if states specifically identified a transmission rate, FERC could preempt state jurisdiction over the rates end-users paid for the transmission of energy to retail customers. Order 888,

---

4/ "Unbundling" permits competition for energy sales to retail customers by breaking ("unbundling") a monopoly rate for delivery of energy and energy into two rates; one for energy and the other for delivery.

1991-1996 FERC Regulations and Preambles (hereinafter Stats. & Regs.) ¶ 31,036 at 31,980. Pet. App. D-121-D-124.

Second, FERC decided that if a seller of unbundled wholesale energy made use of a local distribution system, FERC -- not the states -- would set the rates that the seller would pay for the use of those local distribution facilities. Pet. App. F-7-F-8. Depending on the level of FERC's rates, this dual regulation of local distribution facilities could invite competitors' suppliers to structure "sham" wholesale sales in order to avoid state jurisdiction. See FPA § 212(h) [directing FERC not to issue orders that induce sham wholesale sales].

Third, FERC preempted the states' rate treatment of power plant costs incurred by utilities to serve retail customers, that may be "stranded" (unrecoverable by utilities) due to competition. While this is another area regulated by the states since well before 1935, FERC asserted that it has authority over the rate treatment of such "retail stranded costs," arising from a customer's choice of a new electric supplier, because of its claimed authority over unbundled retail transmission. Recognizing, however, that states had authority over retail stranded costs, FERC declined to exercise its purported authority unless the state regulatory authority lacked power under state law to address retail stranded costs. In those circumstances, FERC stated it would include in transmission rates power plant costs incurred by utilities under state regulation to serve retail customers. FERC further asserted jurisdiction over utility generation costs that were stranded by retail customers becoming wholesale customers, for instance, through the formation of municipal electric utilities or the expansion of existing ones.[5/] FERC stated that it would be the

---

[5/] An entity that had previously been served by an investor-owned electric utility could decide to municipalize, form its own municipal electric utility, become a wholesale customer, purchase bulk power from the wholesale

primary decision-maker on the recovery of those costs. Pet. App. D-64-D-65, D-80-D-84, E-24-E-25, E-71-E-74.

C. The D.C. Circuit's Decision

On June 30, 2000, the D.C. Circuit[6/] upheld all aspects of FERC's preemption. Rather than examine whether Congress had intended to allow such preemption, as required by the Supreme Court (e.g., Fidelity Federal Savings and Loan Ass'n v. De la Cuesta, 458 U.S. 141, 162 (1982)), the Panel deferred to FERC's interpretation of the FPA's jurisdictional limitations. Opn. at 30-31. Pet. App. C-33 to C-34.

In upholding FERC's preemption of state regulation of retail transmission, the Court below read Federal Power Comm'n v. Florida Power & Light Co. (FP&L), 404 U.S. 453 (1972) and Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61, 73 (1943), Opn. at 28-30, Pet. App. C-30-C-31, as holding that FERC had jurisdiction over all unbundled transmission of electric energy on interconnected grids, even transmissions from a generator in the center of a state to a retail customer next door to the generator's plant. Opn. at 28-31. Pet. App. C-30-C-34. Reasoning in the alternative, the D.C. Circuit noted that it felt FERC's interpretation of the FPA's jurisdictional limitations was entitled to deference. Opn. at 31, Pet. App. C-33-C-34.

FPA Section 201(b)(1) denies FERC authority over "facilities used in local distribution," "except as specifically provided in this

---

market, and resell power to its inhabitants. In that case, utility costs previously incurred to serve the area (such as installed generating capacity) could be stranded.

[6/] The relevant portions of the D.C. Circuit's decision on transmission and distribution jurisdiction were written by Judge Sentelle. Stranded cost issues were addressed by Judge Tatel. Slip Opinion "Opn." 4. Pet. App. C.

subchapter and subchapter III" [16 U.S.C. § 824(b)(1)]. Opn. at 31-32, Pet. App. C-34 to C-35. Working from an assumption that § 201(a)'s grant of power to FERC over wholesale sales overrides § 201(b)(1)'s directive that FERC not regulate local distribution facilities (Opn. at 34, Pet. App. C-37), the D.C. Circuit upheld FERC's preemption of state regulation of local distribution facilities.

The D.C. Circuit also (1) decided FERC could "backstop" state decisions on the rate treatment of power plant costs stranded as a result of retail competition and (2) held that FERC could be the "primary forum" for recovery of costs stranded as a result of the loss of retail customers to wholesale competition. Opn. at 73-76, 80-85, Pet. App. C-80 to C-84, C-87 to C-93.

REASONS FOR GRANTING THE WRIT

The D.C. Circuit's decision conflicts with numerous decisions of this Court. It also raises extremely important questions, which go to the heart of a 65-year-old federal/state dual regulatory scheme. One such question is whether a statute designed to preserve state authority and to limit federal regulation to matters that could not be regulated by the states can be used to preempt state jurisdiction over services traditionally regulated by the states.

The Supreme Court consistently has articulated a stringent legal standard for determining whether federal law allows preemption of state law. Where federal agency action preempts activities traditionally regulated by the states, the Court "'start[s] with the assumption that the historic police powers of the States were not to be superseded ... unless that was the clear and manifest purpose of Congress.'" Hillsborough County, Florida v. Automated Medical Labs., Inc., 471 U.S. 707, 715 (1985) (quoting Jones v. Rath Packing Co., 430 U.S. 519, 525 (1977)); Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n,

461 U.S. 375, 383 (1983). The Hillsborough standard is on point, but even if it did not apply, this case would raise the question whether the teaching of Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984), calling for deference to agency readings of statutes they enforce, should extend to an agency's construction of a statute that expressly limits its authority. The Court below held that FERC should receive deference in construing provisions of the Federal Power Act that circumscribe its powers. Opn. at 30-31, Pet. App. C-33-C-34.

The FPA was enacted to fill the "Attleboro gap" and leave untouched state authority over intrastate retail services. FERC has relied upon expanded interconnection by utilities to override Congress' limitation and claim jurisdiction over utility deliveries of energy from generators to consumers in the same state. In so doing, FERC has misapplied this Court's decisions in Federal Power Comm'n v. Florida Power & Light Co., and Jersey Central, which upheld federal jurisdiction over limited aspects of utility operations, not over intrastate retail transactions on utility systems.

The D.C. Circuit's decision also ignored the decisions of this Court that the Federal Power Act simply filled the "Attleboro gap" and otherwise preserved state power over the regulation of utilities. FPC v. Southern California Edison Co., 376 U.S. 205 (1964); Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375, 394 (1983).

Another important question is whether the FERC can undermine state authority to ensure reliable and reasonably priced electricity by overriding the FPA's prohibition of federal regulation of local distribution facilities when electric providers structure electric sales as sales for resale. The D.C. Circuit's decision ignores the FPA's preservation of state authority over

local distribution systems and its prohibition of sham wholesale sales that would defeat state jurisdiction.

Finally, the D.C. Circuit's decision raises a question as to whether FERC may cross the "bright line" created by this Court's decision in FPC v. Southern California Edison and assert jurisdiction over generation costs incurred to provide retail service.

ARGUMENT

POINT I

THE DECISION ALLOWING FERC TO PREEMPT THE STATES' REGULATION OF THE TRANSMISSION OF ELECTRICITY FROM A GENERATOR TO A RETAIL CUSTOMER IN THE SAME STATE CONFLICTS WITH THIS COURT'S TEACHING IN HILLSBOROUGH, IMPERMISSIBLY DEFERS TO FERC'S READING OF THE STATUTE LIMITING THAT AGENCY'S JURISDICTION AND CONFLICTS WITH CONGRESS' RESERVATION OF STATE JURISDICTION OVER INTRASTATE TRANSMISSIONS OF ELECTRICITY

1. As discussed above, this Court has held that where the field that a federal agency seeks to preempt was traditionally occupied by the states "we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." Hillsborough County, Florida v. Automated Medical Labs., 471 U.S. at 715 (1985), quoting Jones v. Rath Packing, 430 U.S. at 525; see Rice v. Santa Fe Elevator Corp.,

331 U.S. 218, 230 (1947) (citations omitted).[7/] It is uncontested that (1) the states were regulating the transmission of electricity from generators to retail customers in the same state when Congress enacted the Federal Power Act (1935 Hearings, FPC Solicitor Devane, at 556, Pet. App. L); and (2) there is no evidence of a clear and manifest intent by Congress to authorize preemption of state regulation. FERC Order 888 at 31,780 (Pet. App. D-42).

Although the states stressed in brief and argument that FERC had not satisfied the Hillsborough standard, the Court below made no mention of Hillsborough, relying instead on a misreading of Chevron U.S.A. Inc. v. Natural Resources Defense Council, 467 U.S. 837 (1984), and a misapplication of Oklahoma Natural Gas Co. v. FERC, 28 F.3d 1281, 1283-1284 (D.C. Cir. 1994) to afford seemingly limitless deference to FERC's interpretation of the Federal Power Act's jurisdictional limitations.[8/] The D.C. Circuit's decision conflicts with Hillsborough as well as numerous decisions of this Court.

[7/] This assumption provides assurance that "the federal-state balance," United States v. Bass, 404 U.S. 336, 349 (1971), will not be disturbed unintentionally by Congress or unnecessarily by the courts.

[8/] Even if the Hillsborough standard of review does not apply, the D.C. Circuit's decision to grant deference to FERC's reading of a federal statute presents a critical issue of state/federal authority, not only because it was made in an area of traditional state authority, but because it was made concerning a statute expressly confining the agency's authority. Throughout its decision, the Court below predicated its decision on deference to FERC's construction of provisions of the Federal Power Act that are designed to cabin that agency's own jurisdiction and reserve jurisdiction to another regulator, i.e., the state public utility commissions (see, e.g., Opn. at 30-31, Pet. App.C-33-C-34) ["it is the law of this circuit that the deferential standard of Chevron U.S.A., Inc. v. Natural Resources Defense Council ... applies to an agency's interpretation of its own statutory jurisdiction" (citation omitted)].

2. The D.C. Circuit's substitution of deference under Oklahoma Natural Gas Co. v. FERC, 28 F.2d 1281 (D.C. Cir. 1994), for the Hillsborough standard and its willingness to render nugatory, by FERC's own admission, FPA § 201(c), present the following, exceptionally important question: may courts uphold federal preemption of long-standing state regulation based not on what Congress intended when it enacted the federal agency's enabling statute, but on what they surmise, in this case incorrectly, to be a federal/state balance that best advances the public interest?

It is vitally important that the Court review this case to answer this question in the negative, and affirm that traditional state police power regulation cannot be shunted aside based on federal agency rules rather than explicit congressional direction. This case uniquely presents the question of deference in the context of a federal agency rule that has usurped more than eight decades of state regulation of electric service.

3. The D.C. Circuit upheld FERC's position that (a) Congress granted FERC jurisdiction of interstate transmissions of electricity; and (b) this Court's decision in Florida Power & Light, plus increased interconnection between utilities in different states, render interstate all transmissions of electricity. It is the second premise -- regarding Florida Power & Light and increased interconnection -- that is fraught with error.

4. The D.C. Circuit's reliance on Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1972), as supporting FERC jurisdiction over all transmissions of electricity on interconnected grids is terribly misplaced. In that case, which did not involve federal preemption of state regulation, the Supreme Court held that the Federal Power Commission had authority to examine the books of a Florida utility because one or more electrons from Florida Power & Light's facilities flowed out of state. 404 U.S. at 454, 461. The Court's conclusion that

some electrons on the utility's system flowed in interstate commerce did not, however, suggest, even remotely, that every electron on Florida Power's system was in interstate commerce. Yet, based perhaps on FERC's assurance that Florida Power was dispositive (FERC Brief at 67-69), the Court below read Florida Power's holding that FP&L transmitted some electrons in interstate commerce as a holding that all electrons carried by all interconnected utilities are in interstate commerce. Opn. at 29-30 (Pet. App. C-32 to C-33). The D.C. Circuit's inductive expansion of Florida Power equates to an argument that because humans have white blood cells and John Smith is a human, all of John Smith's blood cells are white. It is fallacious. Just as the existence of white blood cells in human beings does not render red blood cells non-existent, the fact that some electrons cross state lines does not render transmissions from generators to customers in the same state interstate (See FPA § 201(c) [which states that only transmissions from generators to customers in different states are interstate]).

5. FERC also assured the D.C. Circuit that Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61, 73 (1943), supported preemption. Opn. at 28-29, Pet. App. C-30 to C-32. The Supreme Court in Jersey Central concluded that some electrons of the utility flowed in interstate commerce, but it noted "that although a company may be a public utility under subsection (e), all of its transactions do not thereby fall under the regulatory power of the Commission" (emphasis added). 319 U.S. at 73; see 1947 Hearings, at 553-554. Pet. App. M-29. Indeed, the Court in Jersey Central stressed that § 201(a), which limits FERC jurisdiction to activities not regulated by the states, "is directed to generation, transmission and sale ..." of electricity (emphasis added). 319 U.S. at 74. The Court below, in direct conflict, declined to apply § 201(a) to transmission.

6. FERC's, and subsequently the D.C. Circuit's, reliance on FP&L and Jersey Central to justify FERC's preemption of retail

transmission, stands in stark contrast to repeated statements, some under oath, by the FPC that FP&L and Jersey Central have no relevance to the states' jurisdiction over intrastate rates and services.

In 1947, after Jersey Central prompted a proposal by state commissions to amend the Federal Power Act, the FPC testified the amendment was unnecessary, assuring Congress that "regulation of retail rates and local services is left to the states by the present act even where the energy moves in interstate commerce" (emphasis added). 1947 Hearings, Testimony of FPC Chairman Nelson Smith, at 336, Pet. App. N-14.[9/]

In 1967, after the Fifth Circuit decision in FP&L, FERC testified that a proposed amendment to protect state jurisdiction was unwarranted because "the accounting situation (such as the one in FP&L) differs from rate jurisdiction ....", 1967 Hearings, Testimony of FPC Chairman Lee C. White, at 125, Pet. App. H-15. Moreover, FERC stated in its brief to the Supreme Court in FP&L that an affirmance of its order would only empower it to order FP&L interconnection (§ 202), review mergers and financing (§§ 203, 204) and regulate wholesale rates (§§ 201(b), 205) (FERC FP&L Br., 23, 24, Pet. App. O-3 to O-4). Citing FPC v. Southern Cal., 376 U.S. at 210-216, and the FPA's legislative history, FERC readily acknowledged that it could not regulate retail matters (FERC FP&L Br., 21, 31, Pet. App. O-2, O-10). Contrast such assurances with FERC's insistence in this case that FP&L supports FERC preemption of all unbundled transmission (FERC D.C. Circuit Br.).

7. In ignoring FERC's inconsistency regarding Florida Power and Jersey Central, the D.C. Circuit lost sight of this Court's

---

[9/] House of Representatives Report No. 1318 (1935), at 8, stated that "the [Federal Power] Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce" (emphasis added).

recent teaching that a federal agency's prior assurances to Congress are, indeed, relevant to subsequent jurisdictional disputes. Food and Drug Administration v. Brown and Williamson Tobacco Corp., ___ U.S. ___, 120 S. Ct. 1291, 1312-1314 (2000). The D.C. Circuit also failed to apply the doctrine of judicial estoppel, in conflict with decisions by other circuits. That is, FERC, having taken the position in its Brief in Florida Power & Light that Florida Power & Light and Jersey Central do not preempt state jurisdiction, is estopped from arguing the opposite. Iowa Utilities Board v. Federal Communications Comm'n, 219 F.3d 744, 756 (8th Cir. 2000). In any event, the D.C. Circuit's decision misreads Florida Power and Jersey Central. Neither decision supports FERC preemption of retail transmission.

8. The D.C. Circuit's conclusion that all electricity transmissions are interstate renders meaningless FPA §§ 201(a), (b), (c), § 205 and § 212(h) and ignores 201(c)'s limitation on 201(b) (see American Textile Mfrs. Inst. v. Donovan, 452 U.S. 490, 513 (1981)) [all parts of a statute should be afforded meaning]; Schreiber v. Burlington Northern, Inc., 472 U.S. 1, 8 (1985) [all parts of a statute should be read in pari materia]).

Section 205 allows FERC to regulate only "the transmission or sale of electric energy subject to the jurisdiction of the Commission" (emphasis added). Section 201(a) provides that federal jurisdiction shall "extend only to those matters which are not subject to regulation by the states." The Supreme Court has held that "[§ 201(a)'s] limitation is directed at ... transmission and sale ...." Jersey Central, 319 U.S. at 74-75. If §§ 205 and 201(a) and Jersey Central leave any doubt that FERC cannot preempt state regulation of retail transmissions from generators to customers in the same state (which are most transmissions), § 201(b) and (c) -- together -- state that FERC's jurisdiction shall apply only to the transmission of electric energy "transmitted

from a State and consumed at any point outside thereof" (emphasis added) (§ 201(c)).

Congress would not have specified that FERC's transmission jurisdiction was limited to energy "transmitted from a state and consumed at any point outside thereof" (FPA § 201(c)) if it intended FERC to regulate the transmission of all energy. When the term "interstate commerce" in § 201(b) is read with § 201(c)'s definition of interstate commerce, as it must be, FERC preemption must be rejected because, having jurisdiction only of the transmission of electricity "transmitted from a state and consumed at any point outside thereof" (§ 201(c)), FERC cannot preempt state regulation of transmission from a generator to a retail customer in the same state.[10/]

9. FERC's position runs contrary not only to the FPA as enacted in 1935, but to subsequent amendments added in 1992. Section 212(h) provides that "[n]othing in this subsection shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an ultimate consumer." Thus, Congress not only expressly prohibited FERC from regulating matters, such as retail transmission, that were being regulated by the states in 1935 (§ 201(a)), and prohibited FERC from regulating the transmission of electricity from a generator to a retail customer in the same state (§ 201(b) and (c)), but it has recently declared that no provision in the subsection should be read as affecting the authority of any state over the transmission of electric energy to retail customers (§ 212(h)). The Panel's deference to FERC's position that 201(b) allows it to override all state laws regarding retail transmission directly conflicts with 212(h)'s unequivocal directive.

10/ FERC essentially conceded this point in acknowledging that its preemption decision rendered § 201(c) nugatory, except for Alaska, Hawaii and Texas, (FERC D.C. Circuit brief at 67).

10. FERC's position that all transmission is subject to its jurisdiction also broadsides the admitted purpose of the FPA, which was to fill the "Attleboro gap" (the regulation of interstate transmission and sale of electricity). This Court has held that Congress adopted the test developed in Attleboro. FPC v. Southern California Edison Co., 376 U.S. at 214. The Attleboro test clearly would have allowed states to control retail intrastate transactions, including transmission to retail customers. Indeed, the states regulated such sales in 1935 and thereafter.

11. The D.C. Circuit's conclusion that FERC may preempt state jurisdiction over intrastate retail transmissions conflicts with Federal Power Comm'n v. Southern Cal. Edison Co, 376 U.S. 205, 215 ["Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis"], and the recent decision in Northern States Power Co. v. Federal Energy Regulatory Comm'n, 176 F.3d 1090, 1096 (8th Cir. 1999), rehearing denied, 1999 U.S. App. LEXIS 23493 (8th Cir. 1999), cert. denied, 120 S. Ct. 1221, ___ U.S. ___ (2000) [FERC's "attempt to regulate the curtailment of electric transmission on native/retail consumers is unlawful" under the "bright line"].

12. Rather than analyze §§ 201(b)(c), 205, 212(h), or the ample evidence of Congressional intent to safeguard state regulation, the Court below pointed to increased interconnection between electric utilities after enactment of the FPA as a basis for upholding FERC preemption. Opn. at 24-26, Pet App. C-26 to C28. As a threshold matter, technological changes after Congress has ruled cannot expand an agency's jurisdiction beyond the limits set by Congress. Chemehuevi Tribe of Indians v. Federal Power Comm'n, 420 U.S. 395, 422-424 (1975); Henry v. Federal Power Comm'n, 513 F.2d 395, 401-402 (D.C. Cir. 1975). Further, although the grid in 1935 was less sophisticated than today, it was sufficiently interconnected to allow 18% of all energy to be imported from other states. 74th

Congress, 1st Session: Senate Report No. 621, at 17, House Report No. 1318, at 7, Pet. App. P-1. Finally, this Court has held that mere interconnection of electric utilities is not enough to defeat state jurisdiction. Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n, 461 U.S. 375, 394 (1983).

13. The D.C. Circuit's decision was apparently driven by its view that the electric industry is involved in a transition toward increased competition and that, as the Panel stated, this is an "age of interconnected transmission grids, and ... accompanying technological complexities ...." Opn. at 31, Pet. App. C-34. No basis whatsoever is provided by this claim to infer that Congress' line-drawing can be ignored or to endorse FERC's unauthorized decision to redraw those lines. FERC's preemption of established state regulatory jurisdiction and authority is not in any sense "pro-competitive." Indeed, FERC's position has the effect of discouraging states from implementing retail competition and otherwise serving as regulatory laboratories for national progress. A state that unbundles retail service and thereby provides for competition will lose its jurisdiction over retail transmission service. Retail customers will be deprived of their accustomed state forum and have to seek relief in Washington.

14. Moreover, FERC's attempted seizure of the regulatory authority explicitly conferred on the states by Congress is at odds with this Court's antitrust holdings, the body of law most directly concerned with competition. As the Court held in California v. ARC America Corp., 490 U.S. 93 (1989), federal antitrust laws do not preempt cases brought under applicable state antitrust laws, even though the same alleged conduct may have sufficient impact upon interstate commerce to support a federal antitrust action. The Court noted that there was no explicit Congressional intent to preempt state antitrust laws and that the federal antitrust laws were intended to supplement, not displace, state antitrust laws. The analogy to this case is telling. This

Court should grant certiorari to maintain the jurisdictional dividing lines, just as it did in California v. ARC America Corp. Where a state has exercised its traditional state police powers to protect the welfare of its citizens, State authority should not be overridden, absent explicit preemption by Congress. Hillsborough, supra, California v. ARC America, Corp. supra, see Medtronic v. Lohr, 518 U.S. 484 (1996).

POINT II

THE DECISION THAT FERC MAY PREEMPT STATE REGULATION OF UTILITIES' LOCAL DISTRIBUTION SYSTEMS WHEN ENERGY IS RESOLD CONFLICTS WITH CONGRESS' DIRECTION THAT LOCAL DISTRIBUTION OF ELECTRICITY BE REGULATED BY THE STATES

1. The Court below concluded that § 201(a)'s grant to FERC of authority over wholesale sales overrides § 201(b)(1)'s directive that FERC not regulate local electric distribution systems. Opn. at 34, Pet App. C-37. It thereby allowed FERC to usurp state power to ensure reliable local distribution of electricity over hundreds of thousands of miles of poles, wires and transformers.[11/]

The decision conflicts with Connecticut Light & Power v Federal Power Comm'n, 324 U.S. 515, 531 (1945) where this Court rejected a very similar argument. In that case, the Supreme Court held that the nature of the energy being carried

---

[11/] There are 2,509,620 miles of distribution circuits in the continental United States (Edison Electric Institute 1998 survey data).

over local facilities has no relevance to § 201(b)(1)'s jurisdictional limitation:

> [Section 201(b)(1)] is the provision which loomed importantly in the minds and speech of its sponsors, perhaps was necessary to get the bill passed, and is one which the Commission must observe and the courts must enforce .... It does not seem important whether out-of-state energy gets into local distribution facilities. They may carry no energy except extra-state energy and still be exempted under the Act. The test is whether they are local distribution facilities.

Connecticut Power & Light, 324 U.S. at 529, 531.

The Court below, therefore, erred in reasoning that FERC may regulate the rates charged by utilities for their use of local distribution facilities if the energy being transmitted over the local facilities will be resold. See Duke Power Co. v. Federal Power Comm'n, 401 F.2d 930, 939 (D.C. Cir. 1968) [wherein the D.C. Circuit itself noted that § 201(b) was added to remove any possibility of FERC claiming that it could regulate "facilities used for local distribution"]; Wisconsin-Michigan Power Co. v. Federal Power Comm'n, 197 F.2d 472, 477 (7th Cir. 1952) ["'[f]acilities used in local distribution' means facilities used for making resale and distribution to consumers, jurisdiction over which is left to the states"].

2. Admittedly, FERC does have power to define what is a local distribution system. FPC v. Southern California Edison Co., 376 U.S. at 210, n. 6. There is nothing, however, in this Court's decisions that permits FERC to define "local distribution system" and then declare that definition will not be followed. In adopting a definition for purposes of defining the

transmission/distribution split, FERC is bound to respect state jurisdiction over facilities defined as local distribution.

3. The D.C. Circuit's decision that FERC may preempt state regulation of the rates utilities charge for the use of local distribution facilities to complete wholesale sales presents extremely important questions because it renders § 201(b)'s express language meaningless and undermines the states' ability to protect the reliability of local distribution service. FERC's decision allows electric providers to structure their transactions to evade state consumer service protections and rate recovery of costs necessary to ensure reliable local distribution of electricity.

4. Moreover, the Court below ignored Congress' prohibition against sham wholesale transactions; that is, sales to wholesalers that are really disguised sales to retail customers.[12/] In contravention of that prohibition, FERC's order specifically sanctions sales under federal transmission tariffs by competitive providers that structure their transactions to make a wholesale purchase at an end-user's meter and then turn around and resell electricity at that meter. In bypassing state local distribution tariffs and charges, such transactions clearly violate Congress' prohibition against sham wholesale sales and its intent that state authority over local electric distribution systems be protected.

12/ Federal Power Act Section 212(h) states that "[n]o order issued under this chapter shall be conditioned upon or require the transmission of electric energy ... (2) to, or for the benefit of, an entity if such electric energy would be sold by such entity directly to an ultimate consumer unless [exceptions listed not relevant herein]."

POINT III

THE HOLDING THAT FERC MAY PREEMPT STATE AUTHORITY OVER UTILITY COSTS INCURRED UNDER STATE SUPERVISION TO SERVE RETAIL CUSTOMERS VIOLATES CONGRESS' RESERVATION OF RETAIL ELECTRIC JURISDICTION TO THE STATES

1. With regard to utility generation costs that may become unrecoverable ("stranded") when retail customers reduce purchases from utilities due to competition, the Court below reasoned that FERC could "backstop" state decisions on recovery of stranded costs originally reflected in state-jurisdictional retail rates because (1) FERC's assertion of jurisdiction over retail stranded costs did not impinge on state jurisdiction over rates (Opn. at 74-75, Pet. App. C-81 to C-83), and (2) while in most cases, allowing stranded costs related to generation facilities in transmission rates would not be a legitimate exercise of FERC's authority, it was permissible in the "highly unusual circumstances of this case [open access]." Opn. at 75, Pet. App.C-83. The D.C. Circuit's decision runs contrary to the FPC v. Southern Cal. Edison (Colton) "bright line." That bright line over retail service favors state jurisdiction over retail stranded costs.

2. The D.C. Circuit's first rationale fails because federal agencies cannot trivialize state rate decisions by preempting the cost allocations that govern the revenue requirements addressed by the statute. See Louisiana Pub. Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355, 373-375 (1986) [FCC could not preempt the states' regulation of intrastate depreciation charges]; see also Nantahala Power and Light Co. v. Thornburg, 476 U.S. 953, 967-969 (1986) [although allocations of wholesale costs by FERC, for the purpose of setting wholesale rates bind

the states, the states set retail revenue requirements for retail rate purposes]. The Court below cited Mississippi Industries v. Federal Energy Regulatory Commission, 808 F.2d 1525, 1543-1545 (D.C. Cir. 1987) for the proposition that generation costs can be recovered in FERC-jurisdictional rates, Opn. at 74-75, Pet. App. C-81 to C-82, but inasmuch as that case involved wholesale rates, it does not support a conclusion that FERC may move retail stranded costs into a FERC transmission revenue requirement.

3. The second prong of the Court's reasoning is also incorrect. If utility X spends $500 million on a power plant to serve customers and 10% of the customers opt for generation alternatives, "stranding" $50 million of X's investment, the cause of X's revenue loss, whether it be "open access" (utility X's willingness to carry a competitor's electricity to its customers) or customers installing their own mini-generators, does not transform the stranded generation costs into transmission, or distribution, costs. Indeed, given that an "open" local distribution system is as much of a sine qua non to retail competition as an open transmission system, a percentage of stranded generation costs, under the D.C. Circuit's reasoning, should be considered retail distribution costs, which are regulated solely by the states.

4. The D.C. Circuit concluded that FERC has not interfered with state legislative decisions because it will only act where state commissions have no authority to address stranded cost recovery. Opn. at 76, Pet. App. C-83-C-84. FERC's decision to "backstop" the states denies state legislatures the discretion to design innovative solutions to local problems. For example, a state legislature cannot allow utilities recovery of only a portion of stranded costs in return for a higher rate of return or accelerated return on capital, because of the risk that, notwithstanding the return concessions, FERC will allow recovery of the remaining stranded costs. That FERC may, in

effect, set aside decisions of state legislatures on recovery of stranded costs conflicts with Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989), wherein the Court stated "[i]t cannot seriously be contended that the Constitution prevents state legislatures from giving specific instructions to their utility commissions." 488 U.S. at 313.

5. Finally, the Court below concluded that FERC properly decided it was the "primary forum" for addressing utility generation costs stranded by the formation of municipal utilities because FERC's open access decision makes municipalization feasible and FERC will require a direct nexus between stranded costs and municipalization. Opn. at 82, Pet. App. C-90. The D.C. Circuit, however, never explained why municipalization -- a century old phenomenon by which retail customers of a utility company are served by a newly formed municipal utility -- creates FERC jurisdiction to permit inclusion of stranded retail generation costs in wholesale transmission rates.

6. Because (a) the states, not FERC, are able and willing to address retail customers' rates, and (b) Congress has never indicated a willingness to override state legislative discretion on the rate treatment of costs incurred to serve retail customers, the D.C. Circuit's decision that FERC may preempt state regulation of the rate recovery of "retail stranded costs" raises an extremely important question.

CONCLUSION

As this Court has noted, it is the exclusive province of Congress to rewrite statutes. Louisiana Pub. Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. at 376 (1986). The D.C. Circuit, to the detriment of consumers, has deferred to a FERC reading of the Federal Power Act that renders meaningless several provisions wherein Congress safeguarded state authority over intrastate and retail electric rates and service. The Court should grant the Petition for Certiorari to review the D.C. Circuit's decision upholding FERC's transgressions of its jurisdictional limitations, which significantly undermine the longstanding dual regulatory system that has successfully served our nation's electricity customers for decades.

Respectfully submitted,

Lawrence G. Malone
General Counsel
NYS Public Service Commission
3 Empire State Plaza
Albany, New York 12223-1350
(518) 474-2510

Jonathan D. Feinberg
Diane T. Dean
of Counsel

Dated: October 11, 2000
Albany, New York

APPENDIX A

Order of United States Court of Appeals for the District of Columbia Circuit filed August 22, 2000

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 97-1715 September Term, 1999

Transmission Access Policy Study Group,
Petitioner

v.

Federal Energy Regulatory Commission,
Respondent

Vermont Department of Public Service, et al.,
Intervenors

Consolidated with 98-1111, 98-1112, 98-1113, 98-1114, 98-1115, 98-1118, 98-1119, 98-1120, 98-1122, 98-1124, 98-1125, 98-1126, 98-1127, 98-1128, 98-1129, 98-1131, 98-1132, 98-1134, 98-1136, 98-1137, 98-1139, 98-1140, 98-1141, 98-1142, 98-1143, 98-1145, 98-1147, 98-1148, 98-1149, 98-1150, 98-1152, 98-1153, 98-1154, 98-1155, 98-1156, 98-1159, 98-1162, 98-1163, 98-1166, 98-1168, 98-1169, 98-1170, 98-1171, 98-1172, 98-1173, 98-1174, 98-1175, 98-1176, 98-1178, 98-1180

BEFORE: Edwards, Chief Judge; Silberman, Williams, Ginsburg, Sentelle, Henderson, Randolph, Rogers, Tatel and Garland, Circuit Judges

ORDER

Upon consideration of petitioners' petition for rehearing en banc, and the absence of a request by any member of the court for a vote, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk
By: s/Robert A. Bonner
Robert A. Bonner
Deputy Clerk

Circuit Judges Silberman and Henderson did not participate in this matter.

Filed On: UNITED STATES COURT OF APPEALS
FOR DISTRICT OF COLUMBIA CIRCUIT
Filed: AUG 22 2000
Clerk

APPENDIX B

Judgment of United States Court of Appeals for the District of Columbia Circuit filed June 30, 2000

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 97-1715 September Term, 1999

Transmission Access Policy Study Group, et al.
Petitioner

v.

Federal Energy Regulatory Commission,
Respondent

Vermont Department of Public Service, et al.,
Intervenors

Consolidated with 98-1111, 98-1112, 98-1113, 98-1114, 98-1115, 98-1118, 98-1119, 98-1120, 98-1122, 98-1124, 98-1125, 98-1126, 98-1127, 98-1128, 98-1129, 98-1131, 98-1132, 98-1134, 98-1136, 98-1137, 98-1139, 98-1140, 98-1141, 98-1142, 98-1143, 98-1145, 98-1147, 98-1148, 98-1149, 98-1150, 98-1152, 98-1153, 98-1154, 98-1155, 98-1156, 98-1159, 98-1162, 98-1163, 98-1166, 98-1168, 98-1169, 98-1170, 98-1171, 98-1172, 98-1173, 98-1174, 98-1175, 98-1176, 98-1178, 98-1180

On Petitions for Review of Orders of the
Federal Energy Regulatory Commission

Before: SENTELLE, RANDOLPH and TATEL, *Circuit Judges.*

JUDGMENT

These causes came on to be heard on the petitions for review of orders of the Federal Energy Regulatory Commission and were argued by counsel. On consideration thereof, it is

ORDERED and ADJUDGED, by the Court, that the petitions for review are granted in part and denied in part, in accordance with the opinion for the Court filed herein this date.

FOR THE COURT:
Mark J. Langer, Clerk
By: s/Robert A. Bonner
Robert A. Bonner
Deputy Clerk

Date: June 30, 2000

Opinion Per Curiam

UNITED STATES COURT OF APPEALS
FOR DISTRICT OF COLUMBIA CIRCUIT
Filed: JUN 30 2000
Clerk

MANDATE
Pursuant to the provisions of Fed. R. App. Pro. 41(a)
ISSUED: 8/30/00
By: E. Brown
ATTACHED: —Amending Order
—Opinion
—Order on Costs

APPENDIX C

Opinion of United States Court of Appeals for the District of Columbia Circuit filed June 30, 2000

C-1

UNITED STATES COURT OF APPEALS

FOR THE DISTRICT OF COLUMBIA CIRCUIT

Argued November 3, 1999 Decided June 30, 2000

No. 97-1715

TRANSMISSION ACCESS POLICY STUDY GROUP, ET AL.

PETITIONER

V.

FEDERAL ENERGY REGULATORY COMMISSION,

RESPONDENT

VERMONT DEPARTMENT OF PUBLIC SERVICE, ET AL.,

INTERVENORS

Bills of costs must be filed within 14 days after entry of judgment. The court looks with disfavor upon motions to file bills of costs out of time.

(2)Consolidated with
98-1111, 98-1112, 98-1113, 98-1114, 98-1115, 98-1118,
98-1119, 98-1120, 98-1122, 98-1124, 98-1125, 98-1126
98-1127, 98-1128, 98-1129, 98-1131, 98-1132, 98-1134,
98-1136, 98-1137, 98-1139, 98-1140, 98-1141, 98-1142,
98-1143, 98-1145, 98-1147, 98-1148, 98-1149, 98-1150,
98-1152, 98-1153, 98-1154, 98-1155, 98-1156, 98-1159,
98-1162, 98-1163, 98-1166, 98-1168, 98-1169, 98-1170,
98-1171, 98-1172, 98-1173, 98-1174, 98-1175, 98-1176,
98-1178, 98-1180

On Petitions for Review of Orders of the
Federal Energy Regulatory Commission

Sherilyn Peterson, John T. Miller, Jr., Robert C. McDiarmid, Stanley C. Fickle, Sara D. Schotland, Jeffrey L. Landsman, Lawrence G. Malone, Jeffery D. Watkiss, Richard M. Lorenzo, Isaac D. Benkin, Wallace E. Brand, Daniel I. Davidson, Cynthia S. Bogorad, Harvey L. Reiter and *Randolph Lee Elliott* argued the causes for petitioners. With them on the briefs were *William R. Maurer, Ben Finkelstein, David E. Pomper, Ronald N. Carroll, John Michael Adragna, Sean T. Beeny, Wallace F. Tillman, Susan N. Kelly, Craig W. Silverstein, A. Hewitt Rose, Bryan G. Tabler, James D. Pembroke, David C. Vladeck, Robert F. Shapiro, Lynn N. Hargis, Wallace L. Duncan, Richmond F. Allan, Alan H. Richardson, Michael A. Mullett, C. Kirby Mullen, Robert A. Jablon, Sara C. Weinberg, John F. Wickes, Jr., Todd A. Richardson, Brian A. Statz, John P. Cook, Charles F. Wheatley, Jr., Christine C. Ryan, Robert S. Tongren, Joseph P. Serio, Barry E. Cohen, Carrol S. Verosky, Jennifer S. McGinnity, Jonathan D. Feinberg, Charles D. Gray, Robert Vandiver, Cynthia Miller, Helene S. Wallenstein, William H. Chambliss, C. Meade Browder, Jr., Mary W. Cochran, Paul R. Hightower, Brad M. Purdy, Gisele L. Rankin, Robert D.*

Cedarbaum, Edward H. Comer, Edward Berlin, (3)*Robert V. Zener, Elizabeth W. Whittle, James H. McGrew, Donald K. Dankner, Frederick J. Killion, Joseph L. Lakshmanan, Stephen C. Palmer, Michael E. Ward, Steven J. Ross, Marvin T. Griff* and *Thomas C. Trauger. Leja D. Courter, Robert E. Glennon, Jr., Neil Butterklee, Zachary D. Wilson, Sheila S. Hollis, Janice L. Lower* and *James B. Ramsay* entered appearances.

John H. Conway, Deputy Solicitor, Federal Energy Regulatory Commission, and *Timm L. Abendroth* and *Larry D. Gasteiger*, Attorneys, argued the causes for respondent. With them on the brief was *Jay L. Witkin*, Solicitor. *Susan J. Court*, Special Counsel, and *Edward S. Geldermann*, Attorney, entered appearances.

Edward Berlin argued the cause for intervenors. With him on the briefs were *J. Phillip Jordan, Robert V. Zener, Edward H. Comer, William M. Lange, Deborah A. Moss, James H. McGrew, Steven J. Ross, Elizabeth W. Whittle, Richard M. Lorenzo, David M. Stahl, D. Cameron Findlay, Peter Thornton, J. Phillip Jordan, Robert V. Zener, Robert C. McDiarmid, Cynthia S. Bogorad, Ben Finkelstein, Peter J. Hopkins, Margaret A. McGoldrick, Jeffery D. Watkiss, Ronald N. Carroll, Sara D. Schotland, Alan H. Richardson, Wallace L. Duncan, Richmond F. Allan, A. Hewitt Rose, Wallace F. Tillman, Susan N. Kelly, John M. Adragna, Sean T. Beeny* and *Randolph Lee Elliott. Edward J. Twomey, Richard P. Bonnifield, Frederick H. Ritts, David L. Huard, Dan H. McCrary, Mark A. Crosswhite, John N. Estes, III, Kevin J. McIntyre, John S. Moot, Clark E. Downs, Martin V. Kirkwood, Robert A. Waters, John T. Stough, Jr., Bruce L. Richardson, Floyd L. Norton, IV, William S. Scherman, Douglas F. John, Gary D. Bachman, Nicholas W. Fels, Robert Weinberg, Robert A. Jablon, Peter G. Esposito, Christine C. Ryan, Sheila S. Hollis, Stephen L. Teichler, James K. Mitchell, Gordon J. Smith, Edward J. Brady, Kevin F. Duffy, Michael P. May,*

Barbara S. Brenner, Michael J. Rustum, Sandra E. Rizzo, Kirk H. Betts, Pierre F. de Ravel d'Esclapon, Glen L. Ortman and *William D. DeGrandis* entered appearances.

(4)Before: SENTELLE, RANDOLPH and TATEL, *Circuit Judges.*

Opinion for the Court filed PER CURIAM[1]:

TABLE OF CONTENTS

I. INTRODUCTION 8

II. FERC'S AUTHORITY TO REQUIRE OPEN ACCESS . . . 12
A. Statutory Challenges: FPA §§ 205 and 206 . . . 16
1. §§ 205 and 206 and *Otter Tail Power Company* 16
2. § 206(a) Procedural and Evidentiary Requirements 19
3. Discriminatory Effect of Order 888 22
B. Constitutional Challenge: Fifth Amendment Takings Clause 25

III. FEDERAL VERSUS STATE JURISDICTION OVER TRANSMISSION SERVICES 26
A. Bundled Retail Sales 29
B. Local Distribution Facilities 34

IV. RECIPROCITY 38
A. Indirect Regulation of Non-Jurisdictional Utilities 39
B. Limitation on Reciprocity 41

[1] Following our normal practice in complex cases, we shared the writing of this opinion. Judge Sentelle wrote Section II, Section III, and Section VII. Judge Randolph wrote Section IV, Section VI, and Section VIII. Judge Tatel wrote Section I, Section V, and Section IX.

V. STRANDED COST RECOVERY PROVISIONS 42
A. Wholesale Stranded Costs 44
1. FERC's Authority to Provide for Stranded Cost Recovery 48
a. Reasonable expectation of continued service 48
(5) b. Sections 206 and 212 of the FPA 50
c. Implications of *Cajun* 53
2. Natural Gas Precedent and Conformance to Cost Causation Principles 54
a. Natural gas precedent: *AGD, K N Energy,* and *UDC* 54
b. Conformance to cost causation principles 59
3. FERC's *Mobile-Sierra* Findings 62
a. FERC's authority to make a generic public interest finding 64
b. FERC's stranded cost public interest finding 66
c. FERC's public interest finding regarding customers 68
4. Availability of Stranded Cost Recovery to Nonjurisdictional Utilities and G & T Cooperatives 69
5. Challenges to Technical Aspects of Order 888's Stranded Cost Recovery Provisions 72
a. POSCR's challenges to the stranded cost formula 73
b. Inclusion of known and measurable costs 74
c. Treatment of energy costs in the market option 75
d. Rescission of notice of termination provision 77
e. Provision for benefits lost 77

B. Retail Stranded Costs 78
1. Stranded Costs Arising from Retail Wheeling 79
a. FERC's jurisdiction over retail stranded costs 80
b. FERC's refusal to assert jurisdiction over all retail stranded costs 84
(6) 2. Stranded Costs Relating to Retail-Turned-Wholesale Customers 88

VI. CREDITS FOR CUSTOMER-OWNED FACILITIES AND BEHIND-THE-METER GENERATION 93

VII. LIABILITY, INTERFACE ALLOCATION, AND DISCOUNTING 98
A. Liability and Indemnification 99
B. Interface Allocation 103
C. Delivery-Point-Specific Discounting 105

VIII. TARIFF TERMS AND CONDITIONS 110
A. Headroom Allocation 110
B. Headroom Prioritization 112
C. Duplicative Charges 112
D. Multiple Control Areas 113
E. Right-of-First-Refusal 114

IX. NATIONAL ENVIRONMENTAL POLICY ACT AND REGULATORY FLEXIBILITY ACT COMPLIANCE 115
A. NEPA Compliance 115
1. Adequacy of Base Case 115
2. Failure to Adopt Mitigation Measures 118
B. Regulatory Flexibility Act Compliance 119

Following two notices of proposed rulemaking, the Federal Energy Regulatory Commission issued Orders 888 and 889 on April 24, 1996.[2] Reflecting the Commission's effort to end (7)discriminatory and anticompetitive practices in the national electricity market and to ensure that electricity customers pay the lowest prices possible, these orders represent, as the Commission described in a later order not before us, "the foundation necessary to develop competitive bulk power markets ...." *Regional Transmission Organizations*, Order No. 2000, 65 Fed. Reg. 810, 812 (2000).

Open access is the essence of Orders 888 and 889. Under these orders, utilities must now provide access to their transmission lines to anyone purchasing or selling electricity in the interstate market on the same terms and conditions as they use their own lines. By requiring utilities to transmit competitors' electricity, open access transmission is expected to increase competition from alternative power suppliers, giving consumers the benefit of a competitive market. Most fundamentally, FERC's open access policies, combined with parallel action now occurring on the state level, are intended to create a market in which customers may purchase power from any of a number of suppliers. A municipality or factory in Florida, for example, will no longer have to purchase power from its local utility but

---

[2] *Promoting Wholesale Competition Through Open Access Nondiscriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, FERC Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996), *clarified*, 76 FERC ¶ 61,009 and 76 FERC ¶ 61,347 (1996) ("Order 888"), *on reh'g*, Order No. 888-A, FERC Stats. and Regs. ¶ 31,048, 62 Fed. Reg. 12,274, *clarified*, 79 FERC ¶ 61,182 (1997), *on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248, 62 Fed. Reg. 64,688 (1997), *on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998); *Open Access Same-Time Information System and Standards of Conduct*, Order No. 889, FERC Stats. & Regs. ¶ 31,035, 61 Fed. Reg. 21,737 (1996) ("Order 889"), *on reh'g*, Order No. 889-A, FERC Stats. & Regs. ¶ 31,049, 62 Fed. Reg. 12,484 (1997), *on reh'g*, Order No. 889-B, 81 FERC ¶ 61,253 (1997).

instead may seek cheaper power anywhere in the country. A customer in Vermont may purchase electricity from an environmentally friendly power producer in California or a cogeneration facility in Oklahoma.

All key players in the electricity market have challenged various provisions of Orders 888 and 889. Their claims range from the hypertechnical to arguments that FERC lacks authority to order open access transmission at all. Finding few defects in the orders, we uphold them in nearly all respects.

I. INTRODUCTION

Historically, vertically integrated utilities owned generation, transmission, and distribution facilities. They sold gen-(8)eration, transmission, and distribution services as part of a "bundled" package. Due to technological limitations on the distance over which electricity could be transmitted, each utility served only customers in a limited geographic area. And because of their natural monopoly characteristics, utilities have been heavily regulated at both the federal and state levels.

Since enactment of the Federal Power Act in 1935, the electricity industry has undergone significant change, both economically and technologically. Economies of scale have justified the construction of large (greater than 500 MW) generation facilities, such as nuclear power plants. Technological advances in the 1970s and 1980s have permitted small plants to perate efficiently as well. *See* Notice of Proposed Rulemaking, *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, FERC Stats. & Regs. ¶ 32,514 at 33,059-60, 60 Fed. Reg. 17,662 (1995) ("Open Access NOPR"). Technological improvements also made feasible the transmission of electric power over long distances at high voltages. *See id.* ¶ 32,514 at

33,060. Alternative power suppliers, such as cogenerators, small power producers, and independent power producers emerged in response to these developments. Constructing and operating generation capacity at prices lower than the embedded generation costs of traditional utilities, these alternative suppliers have created a wholesale market for low-cost power.

The growth of this new wholesale market faced a serious obstacle. "As entry into wholesale power generation markets increased," FERC explained, "the ability of customers to gain access to the transmission services necessary to reach competing suppliers became increasingly important." *Id.* at 33,062. Yet the owners of transmission lines, the traditional utilities that had built the high-cost generation capacity, denied alternative producers access to their transmission lines on competitive terms and conditions. FERC therefore began requiring utilities to file open access transmission tariffs that permitted other suppliers to transmit power over (9)their lines under certain circumstances, such as when a utility sought authorization to merge with another utility or to sell power at market-based rather than cost-based rates.

Then, in 1992, Congress enacted the Energy Policy Act, which amended sections 211 and 212 of the FPA to authorize FERC to order utilities to "wheel" power—*i.e.*, transmit power for wholesale sellers of power over the utilities' transmission lines—on a case-by-case basis. Pub. L. No. 102-486, 106 Stat. 2776, 2915-16 (1992) (codified at 16 U.S.C. §§ 824j-k). FERC "aggressively implemented" amended sections 211 and 212 to " 'facilitate the development of competitively priced generation supply options, and to ensure that wholesale purchasers of electric energy can reach alternative power suppliers and vice versa.' " Open Access NOPR, ¶ 32,514 at 33,064 (quoting Notice of Proposed Rulemaking, *Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, FERC Stats. & Regs.

¶ 32,507 at 32,866, 59 Fed. Reg. 35,274 (1994) ("Stranded Cost NOPR")).

Despite these efforts, a persistent barrier to the development of a competitive wholesale power sale market remained. The Commission found that "utilities owning or controlling transmission facilities possess substantial market power; that, as profit maximizing firms, they have and will continue to exercise that market power in order to maintain and increase market share, and will thus deny their wholesale customers access to competitively priced electric generation; and that these unduly discriminatory practices will deny consumers the substantial benefits of lower electricity prices." Open Access NOPR, ¶ 32,514 at 33,052. Power generators not permitted to use utilities' transmission lines on reasonable terms have no way to transmit their power to customers.

Invoking its authority under sections 205 and 206 of the FPA to remedy unduly discriminatory or preferential rules, regulations, practices, or contracts affecting public utility rates for transmission in interstate commerce, 16 U.S.C. §§ 824d-e, and building on its experience in restructuring the natural gas industry, *see Associated Gas Distribs. v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), the Commission issued Orders (10)888 and 889 to "prevent this discrimination by requiring all public utilities owning and/or controlling transmission facilities to offer non-discriminatory open access transmission service." Open Access NOPR, ¶ 32,514 at 33,052. Orders 888 and 889 mandate what FERC terms "functional unbundling," *i.e.*, separating utilities' wholesale transmission functions from their wholesale electricity merchant functions. Specifically, the orders require utilities to (1) file open access nondiscriminatory tariffs that contain the minimum terms and conditions of nondiscriminatory services prescribed by FERC through its pro forma tariff; (2) take transmission service for their own new wholesale sales and purchases of electric energy under the same terms and conditions

as they offer that service to others; (3) develop and maintain a same-time information system that will give potential and existing transmission users the same access to transmission information that the utility enjoys (called the "Open Access Same-Time Information System" or "OASIS"); and (4) state separate rates for wholesale generation, transmission, and ancillary services. *See* Order 888, ¶ 31,036 at 31,635-36.

In requiring utilities to provide open access transmission, FERC acknowledged the dramatic change the orders would bring about, explaining that "[t]he most critical transition issue that arises as a result of the Commission's actions in this rule-making is how to deal with the uneconomic sunk costs that utilities prudently incurred under an industry regime that rested on a regulatory framework and a set of expectations that are being fundamentally altered." Order 888-A, ¶ 31,048 at 30,346. Known as "stranded costs," these "uneconomic sunk costs" are costs that utilities incurred not only with regulatory approval, but with the expectation of continuing to serve their current customers. These costs will become "stranded" when customers take advantage of open access transmission to purchase cheaper power from suppliers other than their historic utilities. Order 888 affords utilities an opportunity to recover stranded costs from their wholesale requirements customers, but only from those customers who use their utility's transmission service to purchase power from new suppliers, and only if the utility can (11)prove that it had a reasonable expectation of continued service to that customer.

After three rehearing orders, the Commission denied any further rehearing. All petitions for review of Orders 888 and 889 were consolidated and transferred to this circuit. We consider these petitions in this opinion. Section II considers challenges to FERC's authority to require utilities to file open access tariffs as a remedy for undue discrimination. Section III evaluates FERC's conclusion that it lacked jurisdiction to order retail unbundling

yet has jurisdiction over transmission where state commissions have unbundled retail sales. Section IV addresses FERC's authority to require nonpublic utilities to provide reciprocal open access transmission service. Section V considers challenges to Order 888's stranded cost recovery provisions. Section VI evaluates petitioners' arguments relating to credits for customer-owned facilities and behind-the-meter generation. Section VII addresses discounting, interface allocation, and liability. Section VIII evaluates other arguments relating to the terms and conditions of the pro forma tariff. Section IX assesses FERC's compliance with the National Environmental Policy Act and the Regulatory Flexibility Act.

In the end, we affirm the orders in all respects except two: we remand for FERC to explain its treatment of energy costs in the stranded cost market option (Section V.A.5.c) and to provide a reasonable cap on contract extensions under existing customers' right-of-first-refusal (Section VIII.E).

II. FERC's Authority to Require Open Access

Although FERC asserts that "mounting claims of undue discrimination in transmission access" prompted its movement toward open access, the open access requirement of Order 888 is premised not on individualized findings of discrimination by specific transmission providers, but on FERC's identification of a fundamental systemic problem in the industry. Generally, those entities that own or control interstate transmission facilities are vertically-integrated public utilities that also generate and sell electricity. In its 1995 (12)notice of proposed rulemaking, FERC observed that there were at that time approximately 328 public utilities, marketers, and wholesale generation entities with transmission needs, and that approximately 137 of those owned or controlled the transmission facilities. *See* Open Access NOPR, ¶ 32,514 at 33,051. Entry into the transmission market is difficult and restricted, so those utilities that already own transmission

facilities enjoy a natural monopoly over that field. The transmission-owning utilities can use their position to favor their own generated electricity and to exclude competitors from the market, whether by denying transmission access outright, or by providing transmission services to competitors only at comparatively unfavorable rates, terms, and conditions. Utilities that own or control transmission facilities naturally wish to maximize profit. The transmission-owning utilities thus can be expected to act in their own interest to maintain their monopoly and to use that position to retain or expand the market share for their own generated electricity, even if they do so at the expense of lower-cost generation companies and consumers.

Even before Order 888, some transmission-owning utilities voluntarily opened their transmission facilities to third party suppliers and purchasers of electricity; and FPA § 211 explicitly gives FERC the authority to order involuntary wheeling on a case-by-case basis. The Commission decided, however, that relying upon voluntary arrangements and § 211 orders would not remedy the fundamentally anti-competitive structure of the transmission industry. Instead, the Commission concluded, such a piecemeal approach would result in an inefficient "patchwork" of transmission systems nationwide. "The ultimate loser in such a regime is the consumer." Open Access NOPR, ¶ 32,514 at 33,071.

As an alternative, the Commission interpreted the anti-discrimination language of FPA §§ 205 and 206, 16 U.S.C. §§ 824d, 824e (1994), as giving it the authority to impose open access as a generic remedy for its findings of systemic anti-competitive behavior. Invoking that broad authority, in Order 888, FERC requires every transmission-owning public utility within FERC's jurisdiction to file an Open Access (13)Transmission Tariff (OATT) containing minimum terms and conditions for non-discriminatory service and to take transmission service for their own wholesale sales and purchases

of electric energy under those filed OATTs. In other words, this order requires the public utilities to provide the same transmission services to anyone purchasing or selling wholesale power—other public utilities, federal power suppliers and marketers, municipalities, cooperatives, independent power producers, qualifying facilities, or power marketers—as they provide to themselves. The Board of Water, Light and Sinking Fund Commissioners of the City of Dalton (Dalton) operates a municipally-owned utility system which provides electric power to residential, commercial, and industrial consumers in the city of Dalton, Georgia. Dalton obtains transmission services from the Georgia Integrated Transmission System (ITS), which it owns along with public utility George Power Company (GPC) and two other utilities that are not subject to FERC's jurisdiction, and which GPC operates according to the terms of various filed agreements. Puget Sound Energy, Inc. (Puget) is a public utility in the Pacific Northwest, where Bonneville Power Administration, which is not a public utility subject to Order 888's requirements,[3] (14)dominates the electricity transmission market. These two industry petitioners challenge the open access

[3] Bonneville Power Administration (BPA) "is a power marketing agency in the Pacific Northwest that markets power from thirty federal hydroelectric projects constructed and operated by the Corps of Engineers and the Bureau of Reclamation." *In re Bonneville Power Administration, Power Sale and Transmission Rates*, 54 F.E.R.C. ¶ 62,143 (1991). In Order 888, FERC concluded that BPA is not a public utility as defined by Federal Power Act (FPA) § 201(e), and thus is not subject to Order 888's requirements. Order 888, ¶ 31,036 at 31,858. FERC admitted, however, to three circumstances under which it might review BPA's transmission access and pricing policies: (1) if BPA files an open access tariff for review and confirmation under the Northwest Power Act and asks FERC to find that the tariff meets FERC's open access policies; (2) to the extent that BPA "is a transmitting utility subject to a request for mandatory transmission services" under FPA § 211; and (3) to the extent that BPA receives open access transmission from a public utility and is thereby subject to the reciprocity provision in that public utility's pro-forma tariff. *Id.*

requirement of Order 888 on various statutory, constitutional, and other grounds.

Turning first to the FPA itself, Puget and Dalton argue that §§ 205 and 206 do not give the Commission the authority to order open access as a generic remedy; and even if the FPA does give the agency such authority, FERC has failed to satisfy the statutory requirements for invoking it. Dalton also argues that Order 888 itself violates the FPA by discriminating against transmission facility owners who have invested in those assets. Shifting to constitutional concerns, Puget and Dalton, along with amicus curiae Pacific Legal Foundation, maintain that Order 888 violates the Takings Clause of the Fifth Amendment. Finally, Dalton argues that the open access requirements of the OATT interfere with the antitrust conditions of outstanding nuclear licenses, and thus are unlawful. While we consider each of these challenges separately,[4] we hold that Order 888's open access requirement is authorized by and consistent with the FPA and the Takings Clause. We conclude also that Dalton has not yet suffered injury from the alleged conflict between open access and the nuclear license antitrust conditions, and that its complaint on that issue is therefore not yet ripe for judicial review.

[4] The Commission and various intervenors on its behalf argue extensively against our jurisdiction over these issues on the grounds that the petitioners failed, in various ways, adequately to raise their concerns before the agency and to preserve the issues for judicial review. Upon careful review of the record, we can safely conclude without further elaboration that these jurisdictional arguments are without merit, that the Commission has had ample notice and opportunity to address all of the petitioners' various statutory, constitutional, and other challenges to Order 888's open access requirement, and that we have jurisdiction to consider these issues.

A. *Statutory Challenges: FPA §§ 205 and 206*

Section 205 of the FPA broadly precludes public utilities, in any transmission or sale subject to FERC's jurisdiction, from "mak[ing] or grant[ing] any undue preference or advantage to (15)any person or subject[ing] any person to any undue prejudice or disadvantage...." 16 U.S.C. § 824d(b). Section 206 of the FPA further provides in relevant part that

> [w]henever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order.

16 U.S.C. § 824e(a). The statutory issues before us are whether these provisions give FERC the authority to order involuntary wheeling as a generic remedy, and if they do, whether FERC satisfied the procedural and evidentiary requirements imposed by these provisions.

1. *§§ 205 and 206 and* Otter Tail Power Company

The Commission did not write on a blank slate when it interpreted FPA §§ 205 and 206 as giving it the authority to order involuntary wheeling as a generic remedy for systemic anti-competitive behavior. Puget and Dalton argue principally that the

Supreme Court's decision in *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973), controls the disposition of this issue. *Otter Tail* was an antitrust case in which the Supreme Court addressed whether the district court could require Otter Tail Power Company to wheel power for its competitors as a remedy for monopolistic practices. Contrary to the company's arguments, the Supreme Court concluded that the district court's order did not impermissibly conflict with the authority of the Federal Power Commission, FERC's predecessor, because the agency did not have the power itself to order involuntary wheeling under Part II of the FPA, which includes §§ 205 and 206. Puget and Dalton (16)cite various circuit court precedents, including one from this circuit, as construing *Otter Tail* to prevent the Commission from ordering involuntary wheeling as a generic remedy. *See, e.g., Florida Power & Light Co. v. FERC*, 660 F.2d 668 (5th Cir. Unit B Nov. 1981); *New York State Electric & Gas Corp. v. FERC*, 638 F.2d 388 (2d Cir. 1980); *Richmond Power & Light v. FERC*, 574 F.2d 610 (D.C. Cir. 1978). Finally, Puget and Dalton note that subsequent to *Otter Tail*, Congress enacted FPA § 211, 16 U.S.C. § 824j, giving FERC the authority to impose open access on a case-by-case basis to remedy a broad range of problems. The petitioners argue that, if FPA §§ 205 and 206 authorize the Commission to impose open access, and if *Otter Tail* does not prohibit such action, then there was no reason for Congress to enact § 211.

In response, the Commission contends that we should not read *Otter Tail* as limiting its authority under FPA § 206 to remedy discriminatory behavior, since *Otter Tail* was an antitrust case and not an undue discrimination case. The Commission also maintains that the circuit court cases cited by the petitioners are not on point and do not prohibit a generic open access remedy. The Commission points instead to our decision in *Associated Gas Distributors v. FERC*, 824 F.2d 981, 998 (D.C. Cir. 1987) (*AGD*), in which we upheld a similar open access transportation requirement imposed by FERC on natural gas transmission, as

the controlling precedent. Finally, FERC argues that Congress enacted FPA § 211 to broaden its already existing authority to order involuntary wheeling, as FPA §§ 205 and 206 authorize such action only as a remedy for undue discrimination.

We agree with FERC that our decision in *AGD* controls the disposition of this issue. In *AGD*, we reviewed a FERC order imposing open access conditions on pipelines transporting natural gas. *See* 824 F.2d at 997-1001. Considering arguments quite similar to those made by the petitioners here, we concluded that *Otter Tail* does not constrain FERC from mandating open access where it finds circumstances of undue discrimination to exist. *See id.* at 998-99. Turning to relevant circuit precedent, we construed *Richmond Power & Light* as supporting only the proposition that a refusal to (17)provide transmission services to another utility was not *per se* unduly discriminatory and we noted that the court in *Florida Power & Light* expressly left open the question of whether FERC could impose open access conditions as a remedy for anti-competitive behavior. *See id.* at 999. Further, we pointed out that our reading of *Richmond* is consistent with other precedent, specifically *Central Iowa Power Coop. v. FERC*, 606 F.2D 1156 (D.C. Cir. 1979), in which we upheld FERC's use of its authority to prevent undue discrimination to condition its approval of a power-pooling agreement upon removal of membership criteria which denied certain privileges to some but not all participants. *See AGD*, 824 F.2d at 999. Indeed, in *AGD*, we noted that open access relies upon the very same principles that we upheld in *Central Iowa*. *See id.* Although *AGD* addressed open access under the anti-discrimination provisions of the Natural Gas Act (NGA) rather than FPA §§ 205 and 206 , we have repeatedly recognized the similarity of the two statutes and held that they should be interpreted consistently. *See Environmental Action v. FERC*, 996 F.2d 401, 410 (D.C. Cir. 1993); *Tennessee Gas Pipeline Co. v. FERC*, 860 F.2d 446, 454 (D.C. Cir. 1988); *see also Arkansas La. Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981). Thus, *AGD*

counsels the conclusion that, while *Otter Tail* may represent a general rule that FERC's authority to order open access is limited, the FPA, like the NGA, makes an exception to that rule where FERC finds undue discrimination.

Moreover, as in *AGD*, the deferential standard of *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984), governs our review of FERC's interpretation of FPA §§ 205 and 206. *See AGD*, 824 F.2d at 1001. If we agreed with Puget and Dalton that the Supreme Court's *Otter Tail* opinion dictates a particular construction of §§ 205 and 206, then the Commission's contrary interpretation would not be entitled to *Chevron* deference. *See Maislin Indus., U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116, 131 (1990) ("Once we have determined a statute's clear meaning, we adhere to that determination under the doctrine of *stare decisis*, and we judge an agency's later interpretation of the statute against (18)our prior determination of the statute's meaning."). But having concluded that *Otter Tail* does not govern the disposition of this case, we are faced solely with considering the validity of FERC's interpretation of the FPA, a statute that the Commission administers. In *AGD*, we concluded that FERC reasonably interpreted the NGA's ambiguous anti-discrimination provisions as giving it broad authority to remedy unduly discriminatory behavior through a generic open access requirement. *See AGD*, 824 F.2d at 1001. Given the FPA's similar language, we can only reach the same conclusion with respect to Order 888. For all of these reasons, we find that the Commission has the authority under FPA §§ 205 and 206 to require open access as a generic remedy to prevent undue discrimination.

2. *§ 206(a) Procedural and Evidentiary Requirements*

Puget and Dalton next argue that, even if FPA §§ 205 and 206 authorize FERC to impose open access generically, § 206(a) imposes certain procedural and evidentiary requirements for

action which the Commission failed in two separate but related ways to satisfy. First, the petitioners claim that FPA § 206(a) requires substantial evidence of contemporaneous "unjust, unreasonable, unduly discriminatory or preferential" behavior before the Commission can act. The Commission made no finding of discrimination or monopoly control on the part of Georgia Power Company or Puget. None of the applications or complaints filed with the Commission accused these petitioners of unduly discriminatory or anti-competitive behavior. Instead, the Commission premised Order 888 on a generic finding that public utility holders as a group have sufficient monopoly power over the transmission of electricity to engage in unduly discriminatory and anti-competitive practices, and that this condition will worsen in the future. To support its finding, the Commission relied upon unsubstantiated allegations of discriminatory conduct in public comments, its own experience in reviewing applications and complaints, and its own understanding of the incentives for monopolists to behave discriminatorily.

(19)Puget and Dalton additionally assert that FPA § 206(a) requires that the requisite findings of undue discrimination be made in the context of a hearing. Although they concede that a rulemaking proceeding can satisfy the statute's hearing requirement, Puget and Dalton maintain that the rulemaking proceeding nevertheless must clearly identify the challenged activities and actors, and give the accused actors the opportunity to demonstrate that their activities were not unlawful. The petitioners protest that the Commission's notice-and-comment rulemaking process did not afford them such opportunity.

FERC claims the discretion under *NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 293 (1974), to choose between rulemaking and case-by-case adjudication; and FERC contends that its generic rulemaking process fully satisfied the requirements of FPA § 206(a). FERC concedes that it relied upon general

findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. Citing our opinion in *Wisconsin Gas Co. v. FERC*, 770 F.2d 1144, 1166 (D.C. Cir. 1985), however, FERC maintains that such findings are sufficient to substantiate its decision to impose the open access requirement. Finally, FERC observes that we rejected these same arguments in *AGD*. *See* 824 F.2d at 1008 (citing *Wisconsin Gas*, 770 F.2d at 1165-68).

Again, we must agree with the Commission. In *American Public Gas Ass'n v. FPC*, we held that the Commission could exercise its authority under NGA § 5(a), the provision parallel to FPA § 206, through rulemaking as well as adjudication. *See* 567 F.2d 1016, 1064-67 (D.C. Cir. 1977); *See also Wisconsin Gas*, 770 F.2d at 1153 (articulating the *American Public Gas* holding). Congress subsequently ratified the *American Public Gas* holding when it enacted the Department of Energy Organization Act, 42 U.S.C. § 7173(c) (1994). *See Wisconsin Gas*, 770 F.2d at 1153 n.8 (acknowledging the Act). That statute provides that "the establishment of rates and charges under the Federal Power Act [16 U.S.C. 791a et seq.] or the Natural Gas Act [15 U.S.C. 717 et seq.], may be conducted by (20)rule-making procedures." 42 U.S.C. § 7173(c) (brackets in original). By passing a statute adopting the holding of *American Public Gas*, and explicitly applying that rule to the FPA as well as the NGA, Congress signaled its intent that the hearing requirements of NGA § 5(a) and FPA § 206(a) be interpreted similarly.

Interpreting the hearing requirement of NGA § 5(a), we have said that, while the Commission cannot rely solely on "unsupported or abstract allegations," the agency is also not required to make "specific findings," so long as the agency's factual determinations are reasonable. *See Wisconsin Gas*, 770 F.2d at 1158. In *AGD*, we applied *Wisconsin Gas* in holding that the Commission was not required to make specific findings that

individual rates charged by individual pipelines were unlawful, or to offer empirical proof for all the propositions upon which its order depended, before promulgating a generic rule to eliminate undue discrimination. *See AGD*, 824 F.2d at 1008-09. Upon comparison of the order considered in *AGD* with Order 888, if anything, FERC more thoroughly documented the reasons for its actions in Order 888 than in the earlier natural gas order.

Puget claims that *AGD* and *Wisconsin Gas* are distinguishable, and that this case is governed by *Electricity Consumers Resource Council v. FERC*, 747 F.2d 1511 (D.C. Cir. 1984), in which we reversed FERC's adoption of a rate based on an economic theory in the absence of a discussion of the practical applications of that theory. *See* 747 F.2d at 1514. As the *AGD* court recognized, however, the court in *Electricity Consumers* was persuaded that the Commission had distorted the economic theory it claimed to apply. *See AGD*, 824 F.2d at 1008. Just as the pipelines in *AGD* did, Puget has failed to articulate exactly how FERC has distorted the theories on which it relies in Order 888. Additionally, the *AGD* court rejected the idea that "*Electricity Consumer*'s reference to 'economic theory' was intended to invalidate agency reliance on generic factual predictions merely because they are typically studied in the field called economics." *Id.* Following the rationale of *Wisconsin Gas* and *AGD*, we conclude that (21)FERC has satisfied the requirements for invoking its authority under FPA § 206(a).

3. *Discriminatory Effect of Order 888*

Dalton charges that, even if the FPA permits FERC to impose involuntary wheeling generally, the open access requirement of Order 888 causes rather than remedies discrimination, and therefore violates FPA § 206(a)'s express requirement that FERC act against undue discrimination. Specifically, Dalton and the other non-jurisdictional owners of the Georgia ITS facilities invested millions of dollars in those facilities in order to use the

facilities each owns and receive reciprocal open access transmission services from the other owners. Under the Open Access Transmission Tariff (OATT), other customers do not have to make such investments to use the Georgia ITS facilities. FERC responds that Order 888 does not unduly discriminate between old and new customers of integrated transmission systems like the Georgia ITS; and that if Dalton has evidence that the tariff results in undue discrimination in its individual circumstances, Dalton remains free to file a petition under FPA § 206 for redress, and FERC will consider its claim.

FERC's conclusion that its open access requirement is not unduly discriminatory is subject only to arbitrary and capricious review. *See* 5 U.S.C. § 706(2)(A) (1994); *Sithe/Independence Power Partners, LP v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999); *Union Pacific Fuels, Inc. v. FERC*, 129 F.3d 157, 161 (D.C. Cir. 1997). We conclude that FERC has adequately explained why its open access requirement is not unduly discriminatory. Relying upon extensive commentary as well as its own experiences, FERC concluded that, as a general matter, transmission industry conditions were conducive to discriminatory practices and anti-competitive behavior, such that case-by-case adjudication could not adequately address the problem. FERC also recognized that its generic findings may have exceptions, and thus that Order 888 may in individual circumstances have a different result than that intended. Therefore, Order 888 does not preclude facilities owners the opportunity to argue their particular circum-(22)stances in their OATT filings or, as with Dalton, in their own petitions for relief under FPA § 206(a). Rather, Order 888 merely shifts from a regulatory norm in which a user of transmission services must demonstrate to FERC an individualized need for open access to one in which a provider of transmission services must present to FERC individualized circumstances requiring relief from open access. As the petitioners have a mechanism by which they can seek relief for their particular concerns, we find nothing arbitrary

or capricious about FERC's conclusion that its approach to open access is not unduly discriminatory.

In another stab at demonstrating the discriminatory effect of Order 888's open access requirement, Dalton alerts us to an agreement entered into between it and Georgia Power Company (GPC) in partial implementation of antitrust conditions contained in operating licenses issued by the Nuclear Regulatory Commission for jointly owned nuclear facilities connected to the Georgia ITS. Those antitrust conditions require GPC to provide Dalton with transmission services until the nuclear licenses expire, long after the ITS Agreement terminates. Dalton alleges that limitations imposed by Order 888 on Dalton's rights upon termination of the ITS Agreement are inconsistent with GPC's obligations under the nuclear licenses, and that the interference will result in discrimination against Dalton. FERC maintains that it agreed in addressing GPC's Order 888 compliance filing to treat the ITS Agreements separately.

Ultimately, Dalton has offered no present injury from the alleged conflict, so this issue is not ripe for review. Dalton will only be injured if, upon termination of the ITS Agreement, Order 888 interferes with Dalton's right to transmission services. Dalton's own argument suggests as much, observing that FERC "left to GPC the decision whether it 'must, but cannot, comply with separate orders' of NRC and FERC and whether it will present evidence of such conflict to either Commission," and complaining that even if GPC does act, "the orders under review provide no assurance that the competitive transmission and other service rights provided by the nuclear licenses will be respected under the OATT." Br. (23)of Petitioner Dalton at 23 (quoting Order 888-A, ¶ 41,048 at 30,452). In short, GPC and FERC are still in the process of determining whether the antitrust provisions even conflict with Order 888, as well as how to deal

with any such inconsistency.[5] Accordingly, this issue is not appropriate for judicial review at this time.

B. *Constitutional Challenge: Fifth Amendment Takings Clause*

Puget and amicus curiae Pacific Legal Foundation (Pacific) contend that Order 888 violates the Takings Clause of the Fifth Amendment. These petitioners maintain that Order 888's open access requirement engineers a "taking" in two ways: First, that FERC's open access requirement effects a regulatory taking by arbitrarily changing pricing methodology in a way that excessively deprives transmission owners of their investments in facilities; and, second, that the open access requirement allows a physical invasion, a permanent physical occupation, by taking away the transmission owners' right to exclude competitors from their transmission property. We cannot grant relief on either ground.

When the action of the federal government effects a "taking" for Fifth Amendment purposes, there is no inherent constitutional defect, provided just compensation is available. At bottom, both of the petitioners' Fifth Amendment claims turn not on whether open access effects a taking, but whether FERC's cost-based transmission pricing policies in the end provide just compensation. The remedy of just compensation is not within our jurisdiction but that of the United States Court of Federal Claims, under the Tucker Act, 28 U.S.C. § 1491. *See Bell Atlantic Tel. Cos. v. Federal Communications Comm'n*, 24 F.3d 1441, 1444 n.1 (D.C. Cir. 1994); *Railway Labor Executives' Ass'n v. United States*, 987 F.2d 806, 815-16 (D.C. Cir. 1993).

---

[5] GPC's management of the Georgia ITS is subject to the direction of a committee that includes Dalton representatives.

We recognize that our jurisdiction to review an agency's construction of a statute necessarily involves an exercise of (24)the policy of avoiding constitutional issues where possible, even though the issues may concern arguable takings amenable to Tucker Act remedy, "when 'there is an identifiable class of cases in which application of a statute will necessarily constitute a taking.' " *Bell Atlantic*, 24 F.3d at 1445 (D.C. Cir. 1994) (quoting *United States v. Riverside Bayview Homes, Inc.*, 474 U.S. 121, 128 n.5 (1985)). We need not decide whether this case falls within that category, however, because even if it did, any takings problem created by Order 888 does not raise such significant constitutional doubt as to require us to construe the FPA to prohibit FERC from ordering open access. If there is a taking, and a claim for just compensation, then that is a Tucker Act matter to be pursued in the Court of Federal Claims, and not before us.

III. FEDERAL VERSUS STATE JURISDICTION OVER TRANSMISSION SERVICES

Vertically integrated utilities use their own facilities to generate, transmit, and distribute electricity to their customers. Traditionally, the customer paid one combined rate for both the power and its delivery, thus the industry refers to such sales as "bundled." To the extent that bundled sales are made directly to the end user of the electricity, they are also recognized as retail sales. Utilities may also sell the electricity they generate at wholesale to other utilities or other resellers of power, which then resell that power to their own customers. Thus, the same utility may use its facilities to serve both retail and wholesale customers. Vertically integrated utilities use their transmission facilities to move electricity over long distances, and use local distribution lines to deliver the electricity to the end user.

Even before Congress enacted the FPA, the Supreme Court held that states could not regulate wholesale sales of electricity.

See Public Utils. Comm'n of R.I. v. Attleboro Steam & Elec. Co., 273 U.S. 83 (1927). A few years leter in 1935, Congress included in the FPA a provision giving the Federal Power Commission, FERC's predecessor agency, the authority to regulate "the sale of [electric] energy at whole-(25)sale," as well as "the transmission of electric energy in interstate commerce." FPA § 201(a), 16 U.S.C. § 824(a) (1994). FERC also limited federal regulation "to those matters which are not subject to regulation by the States," *id.*, and reserved to the states "jurisdiction ... over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce...." FPA § 201(b), 16 U.S.C. § 824(b). Pursuant to these provisions, FERC has regulated wholesale power sales and interstate transmissions, and state agencies have retained jurisdiction over bundled retail transactions, including service issues and the intrastate sale and distribution of electricity through local distribution facilities.

Initially, as most transactions involved either a wholesale or a retail sale, and correspondingly transmission or local distribution facilities, this regulatory division of labor was straight-forward in application. Indeed, in 1935, when Congress enacted the FPA, the networks of high-voltage, long-distance transmission lines which today crisscross the United States did not exist. Instead, vertically integrated utilities individually built facilities sufficient to meet the power needs of their customers. Over time, however, the landscape of the electric industry changed.

Utilities decided to cover demand spikes by sharing power, rather than by building more generation capacity. The transmission grid developed from these arrangements. Eventually, nonutility generators started producing electricity; and power marketers began to buy and resell electricity to other power marketers, utilities, or even directly to consumers. These

industry participants do not own transmission lines, so they rely upon the utilities that own such facilities to provide transmission services. In addition to their traditional bundled sales activity, vertically integrated utilities started "unbundling" their own services and developing their own power marketing units to buy and sell electricity at wholesale. Some states even mandate unbundling of retail services. As a result of these changes, facilities once used solely for local distribution of bundled retail sales now engage regularly in (26)unbundled wholesale transmissions and retail delivery as well. Thus, while the electricity world once neatly divided into spheres of retail versus wholesale sales, and local distribution versus transmission facilities, such is no longer the case.

In Order 888, FERC reinterpreted FPA § 201 to accommodate the new industry practices and conditions. FERC left the regulation of bundled retail transmissions to the states, concluding that "when transmission is sold at retail as part and parcel of the delivered product called electric energy, the transaction is a sale of electric energy at retail." Order 888, ¶ 31,036 at 31,781. Nevertheless, FERC asserted jurisdiction over all unbundled retail transmissions, and left to the states only the sales portion of unbundled retail transactions, on the ground that FPA § 201 gives it jurisdiction without qualification over all transmission by public utilities in interstate commerce. *See id.* Also, while acknowledging that FPA § 201(b) explicitly places retail transmissions by "facilities used in local distribution" beyond the Commission's jurisdiction, FERC adopted a seven factor jurisdictional test for determining which facilities fall within that category, and claimed exclusive authority over those that do not. *See id.* at 31,780, 31,784. In the present litigation, eachy of these changes is challenged, with some petitioners claiming that FERC went too far, and others contending that the Commission did not go far enough in asserting jurisdiction.

A. *Bundled Retail Sales*

Several state regulatory commissions complain that FERC exceeded the boundaries of its statutory authority by asserting jurisdiction over unbundled retail transmissions. These state petitioners argue that the plain meaning and history of FPA § 201(a) gives FERC the authority to regulate only transmissions of electricity consumed in a state other than that in which the electricity was generated, if the transmission was not otherwise subject to state regulation. The states historically have regulated retail transmissions as part of bundled retail sales of electricity, while FERC has regulated wholesale transmissions; and the division of regulatory jurisdiction should not change merely because those transac-(27)tions have now been unbundled into separate generation, transmission, and sales components.

Two groups of transmission dependent utilities, TAPS and TDU Systems, and the nation's largest power wholesaler, Enron Power Marketing (collectively the "unbundling and discounting" or "U&D" petitioners), both intervene on the side of FERC with respect to the states' claim, and separately challenge FERC's interpretation of its jurisdiction on different grounds. The U&D petitioners contend that FERC impermissibly limited its jurisdiction by leaving the regulation of bundled retail transmissions to the states. These parties maintain that FERC has the authority to regulate both bundled and unbundled retail transmissions, and that FERC violates FPA § 206 by limiting the scope of Order 888 to the latter. To establish that bulk transmission by utilities is transmission in interstate commerce regardless of whether the power is sold at wholesale or retail, the U&D petitioners cite particularly *FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972), and *Jersey Central Power & Light Co. v. FPC*, 319 U.S. 61 (1943), two of the cases relied upon by FERC in the Notice of Proposed Rulemaking, ¶ 32,514 at 33,135-42. As further support that FERC's jurisdiction extends to all interstate transmissions, the U&D petitioners offer NGA

precedent recognizing FERC's authority over all interstate gas transportation, if not the gas being transported. *See, e.g. FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972); *United Distribution Cos. v. FERC*, 88 F.3d 1105, 1153 (D.C. Cir. 1996) (*UDC*); *Mississippi River Transmission Corp. v. FERC*, 969 F.2d 1215 (D.C. Cir. 1992). These petitioners contend that excluding bundled retail transmissions from the OATT will permit discrimination and give owners a competitive advantage, contrary to the mandate of FPA § 206(a) that FERC eliminate undue discrimination. Accordingly, the U&D petitioners claim that FERC erred when it declined to mandate functional unbundling for an owner's transmissions to bundled retail customers of (1) its own generated power or (2) power purchased at wholesale.

In response to these challenges, FERC maintains that the plain meaning of FPA § 201 gives the Commission jurisdic-(28)tion over all interstate transmissions without qualification, while at the same time limiting jurisdiction over sales to wholesale sales. Relying particularly on *Florida Power & Light* and *Jersey Central Power & Light*, FERC asserts broad jurisdiction over all transmission activities in interstate commerce. As for bundled retail sales, FERC's position is that once the transmission service is bundled with generation and local distribution, it becomes merely a component of the retail sale itself, over which FERC has no jurisdiction. FERC maintains that natural gas jurisprudence is inapplicable because the language of the NGA and FPA differ on this issue, and the natural gas cases turned on the existence of a regulatory gap that does not exist in the electricity field. FERC also asserts that its interpretation of the FPA's jurisdictional grant is entitled to deference under *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984).

Both FPA § 201(a) and (b) clearly and unambiguously confer upon FERC jurisdiction over the "transmission of electric energy

in interstate commerce." FPA § 201(c) further provides that "electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof." 16 U.S.C. § 824(c). In both *Florida Power & Light* and *Jersey Central Power & Light*, the Supreme Court considered whether certain indirect transmissions of electrical power across state lines represented transmissions in interstate commerce.

Jersey Central Power & Light involved the transmission of energy generated by Jersey Central in New Jersey. Jersey Central transmitted electricity to the New Jersey transmission facilities of another company, Public Service, which then transmitted the power first to another of its New Jersey facilities, and then on to a facility owned by yet a third company and located in the middle of a body of water separating New Jersey from Staten Island, New York. The third company in the chain then transmitted the energy first to its own facilities in New York, then finally and ultimately to consumers in New York. Jersey Central's own transmission facilities were located solely in New Jersey, and as were (29)the facilities used by Public Service to receive the transmissions from Jersey Central.

The Supreme Court recognized that Jersey Central had no control over the transmissions' destination once the electricity was delivered to Public Service, *see Jersey Central*, 319 U.S. at 65, and that the total flow of electricity from Jersey Central to New York was small. *See id.* at 66. Nevertheless, because some electricity generated by Jersey Central in New Jersey was consumed in New York, the Court upheld FERC's jurisdiction under FPA § 201 over Jersey Central's transmission facilities as utilized for transmissions in interstate commerce. *See id.* at 67. The Court said that, under FPA § 201(a) and (b), FERC's power extends over all facilities "which transmit energy actually moving in interstate commerce." *Id.* at 72. The Court emphasized, however, that "mere connection" of one utility's transmission

facilities to those of another transmitting in interstate commerce was insufficient for jurisdiction under FPA § 201. *Id.*

The Court revisited the issue in *Florida Power & Light*, which involved certain Florida and Georgia utilities who voluntarily connected their transmission facilities to coordinate their activities and exchange power as required to meet temporary needs. Like Jersey Central, FP&L's transmission facilities were confined to Florida, and none of FP&L's transmission lines directly connected with those of out-of-state companies. Nevertheless, because FP&L was a member of a group of interconnected utilities, its transmission lines connected with those of other Florida utilities; and the lines of one of those other utilities, Florida Power Corp., interconnected just short of Florida's northern border with those of Georgia Power Co. Records indicated that power transfers between FP&L and Florida Power coincided with transfers between Florida Power and Georgia Power.

In *Jersey Central*, logs of the relevant companies demonstrated at least a dozen occasions when facilities in New York drew power from certain lines at times when Jersey Central was the only supplier of electricity to those lines. *See Florida Power & Light*, 404 U.S. at 459. By way of contrast, (30)there was no similar evidence that power generated by FP&L specifically passed through Florida Power to Georgia Power, with Florida Power serving as a mere conduit. *See id.* At best, company records demonstrated instances when transfers between FP&L and Florida Power occurred at or about the same time as transfers between Florida Power and Georgia Power. *See id.* at 457.

Instead, the Court considered two theories by which FP&L's power could be deemed transmitted across state lines. The first posited a cause and effect relationship by which every flick of a light switch would cause every generator on a multi-state

interconnected system to produce some quantity of additional electricity to maintain the system's balance, and thus to transmit electric energy throughout the system and across state lines. The second theory suggested that where the transmission lines of two utilities interconnect, their energy commingles, such that inevitably some energy transmitted by FP&L to Florida Power was then transmitted to Georgia Power and across state lines.

Despite its statement in *Jersey Central* that "mere connection determines nothing," 319 U.S. at 72, the Court relied on the second of these theories to conclude that FP&L's facilities were transmitting energy in interstate commerce, and left open the possible validity of the cause and effect theory. *See* 404 U.S. at 462-63. Writing in dissent, Justice Douglas characterized the Court's opinion as "mean[ing] that every privately owned interconnected facility in the United States ... is within the [Federal Power Commission's] jurisdiction," such that otherwise local utilities would now be subject to the mandates of the federal bureaucracy. *Id.* at 471 (Douglas, J., dissenting).

The Supreme Court has interpreted the language in FPA § 201 regarding FERC's jurisdiction over transmissions in interstate commerce. We are bound by the High Court's dictates to conclude that the FPA gives FERC the authority to regulate the transmissions at issue here, whether retail or wholesale. Even if the Court had not so spoken, however, and even if we independently concluded that the statute's text (31)was less than clear, it is the law of this circuit that the deferential standard of *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984), applies to an agency's interpretation of its own statutory jurisdiction. *See Oklahoma Natural Gas Co. v. FERC*, 28 F.3d 1281, 1283-84 (D.C. Cir. 1994). As guided by *Chevron*, unless Congress has directly spoken to the contrary, or FERC has unreasonably or impermissibly interpreted the statute, we must defer to the Commission's construction of ambiguous provisions of the FPA. *See Chevron*, 467 U.S. at 842-43. In this

age of interconnected transmission grids, and given the accompanying technological complexities, we would be hard pressed to conclude that FERC's interpretation of § 201(c) as giving it jurisdiction over both wholesale and retail transmissions is unreasonable or impermissible.

Nevertheless, we are not persuaded that this conclusion requires FERC to mandate unbundling and assert jurisdiction over all retail transmissions. Just as FPA § 201 gives FERC jurisdiction over transmissions in interstate commerce and sales at wholesale, the statute also clearly contemplates state jurisdiction over local distribution facilities and retail sales. The statute is much less clear about exactly where the lines between those activities are to be drawn. A regulator could reasonably construe transmissions bundled with generation and delivery services and sold to a consumer for a single charge as either transmission services in interstate commerce or as an integral component of a retail sale. Yet FERC has jurisdiction over one, while the states have jurisdiction over the other. FERC's decision to characterize bundled transmissions as part of retail sales subject to state jurisdiction therefore represents a statutorily permissible policy choice to which we must also defer under *Chevron*. Accordingly, we affirm FERC's decisions in Order 888 to assert jurisdiction over unbundled retail transmissions while leaving regulation of bundled retail transmissions to the states.

B. *Local Distribution Facilities*

FPA § 201(b) explicitly excludes from FERC jurisdiction "facilities used in local distribution or only for the transmis-(32)sion of electric energy in intrastate commerce." 16 U.S.C. § 824(b) (1). Historically, wholesale sales have not for the most part involved local distribution facilities. FERC claims that increased unbundling gives resellers the opportunity to reconfigure the wholesale sales so that they might now occur on those facilities which traditionally have been treated as local

distribution facilities. Moreover, FERC's assertion of jurisdiction over the transmission component of unbundled retail sales blurred the line between local distribution facilities and facilities used for transmission in interstate commerce.

In Order 888, FERC claimed exclusive authority over the regulation of facilities which sell and transmit electricity at wholesale to customers who will resell the electricity to end users. With respect to unbundled retail sales, FERC acknowledged that transmissions by "facilities used in local distribution" are beyond the Commission's jurisdiction, while facilities engaged in interstate transmission are subject to FERC jurisdiction under FPA § 201(a). Thus FERC adopted a seven factor jurisdictional test to identify whether a facility is a local distribution facility subject to state jurisdiction or a facility engaged in interstate transmission subject to FERC jurisdiction.[6] In short, under Order 888, when a (33)public utility is engaged in wholesale transmission, FERC has jurisdiction regardless of the nature of the facility; but when the public utility is engaged in unbundled retail transmission, the facts and circumstances will

---

[6] The Commission's seven factor test involves evaluating on a case-by-case basis whether the activities of the facilities in question correspond with seven specific indicators of local distribution:

(1) Local distribution facilities are normally in close proximity to retail customers.

(2) Local distribution facilities are primarily radial in character.

(3) Power flows into local distribution systems; it rarely, if ever, flows out.

(4) When power enters a local distribution system, it is not reconsigned or transported on to some other market.

(5) Power entering a local distribution system is consumed in a comparatively restricted geographical area.

(6) Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

(7) Local distribution systems will be of reduced voltage.

Order 888, ¶ 31,036 at 31,981.

determine whether the facilities are subject to FERC or state jurisdiction.

The state petitioners argue that FERC's dual approach radically expands its jurisdiction and violates Congress' explicit directive in FPA § 201(b) that regulation of local distribution facilities be left to the states. The states contend that Congress clearly intended to preserve state jurisdiction over local distribution facilities, regardless of whether the energy comes from out of state or the sale is a wholesale sale. The states maintain that, by claiming jurisdiction over any facility transporting energy for resale, regardless of whether the facility might otherwise be a local distribution facility under the seven factor test, FERC has adopted the circular reasoning that wholesale sales do not occur on local distribution facilities, so any facility that engages in wholesale activities is not a local distribution facility. The states contend further that FERC offers no reasoned analysis of why local distribution should be defined differently for wholesale versus retail sales. The states finally charge that, under Order 888, nearly identical facilities would be under federal jurisdiction and state jurisdiction for different customers receiving indistinguishable service. Such a situation, they contend, will only encourage energy marketers to choose their regulator by using middlemen to shift the point at which title to the power transfers, and thus undermine the jurisdictional certainty that Order 888 states is necessary for competition.

FERC responds that it is not asserting jurisdiction over local distribution facilities, but asserts that when a public utility delivers unbundled energy at wholesale to a supplier for the purpose of resale to an end user, FPA § 201 gives FERC unqualified authority to assert jurisdiction over the facility used to effect that transaction. When the public utility is engaged in unbundled retail transmission, however, (34)the circumstances of a specific case will determine whether the facilities used are subject to FERC or state jurisdiction. The arguments by the

states do no more than raise policy concerns which are for FERC and not the court. *See Arent v. Shalala*, 70 F.3d 610 (D.C. Cir. 1995).

Intervening again on FERC's behalf on this issue, the U&D petitioners add that FERC's use of different tests is appropriate given the differences in the two separate jurisdictional grants of FPA § 201. The interveners argue that, given the statute's clear grant to FERC of jurisdiction over all aspects of wholesale sales, FERC is fully justified in employing a functional test to identify wholesale transmissions. In contrast, because FERC's jurisdiction over retail sales is limited to transmissions in interstate commerce, the seven factor test is more appropriate.

We agree that FERC's dual approach to assessing its jurisdiction stems from the fact that FPA § 201 contains more than one jurisdictional grant. FPA § 201(b) denies FERC jurisdiction over local distribution facilities "*except as specifically provided in this subchapter and subchapter III.*" 16 U.S.C. § 824(b)(1) (emphasis added). FPA § 201(a) makes clear that all aspects of wholesale sales are subject to federal regulation, regardless of the facilities used. FERC's assertion of jurisdiction over all wholesale transmissions, regardless of the nature of the facility, is clearly within the scope of its statutory authority. Moreover, various cases support the proposition that FERC regulates all aspects of wholesale transactions. *See, e.g., Duke Power Co. v. FPC*, 401 F.2d 930. 935-36 (D.C. Cir. 1968) (noting that the FPC regulates public utility facilities used in wholesale transmissions or sales in interstate commerce); *Arkansas Power & Light Co. v. FPC*, 368 F.2d 376, 383 (8th Cir. 1966) (stating that the functional use of the transmission lines—wholesale versus retail—controls); *Wisconsin-Michigan Power Co. v. FPC*, 197 F.2d 472, 477 (7th Cir. 1952) (finding that transmission facilities used at wholesale are not "local distribution facilities").

(35)The seven factor test applies only to unbundled retail sales, where FERC seeks to regulate pursuant to the separate grant of jurisdictional authority over transmissions in interstate commerce. In this context, the definition of "facilities used in local distribution" becomes relevant. The statute does not define "facilities used in local distribution," but instead leaves that task to FERC. As *Chevron* counsels us, FERC's interpretation of undefined and ambiguous statutory terms is entitled to deference. *See Chevron*, 467 U.S. at 842-43.

FERC has adopted a multi-factor test to determine the nature of transmission facilities. In a footnote, Order 888 says that distribution-only facilities which sell only at retail will still be considered local distribution facilities. *See* Order 888, ¶ 31,036 at 31,981 n.99. This is consistent with the fact that states historically have regulated bundled retail sales to end users. However, Order 888 implicitly recognizes the current reality that many primarily retail utilities engage in both local distribution and interstate transmissions, and seeks through the seven factors to discern each facility's primary function. We cannot agree with the state petitioners that this approach is unreasonable or otherwise impermissible.

IV. RECIPROCITY

Section 6 of the Tariff contains a reciprocity provision resting on the principle that any public utility offering "non-discriminatory open access transmission for the benefit of customers should be able to obtain the same non-discriminatory access in return." Order 888, ¶ 31,036 at 31,760. Non-public utilities—those outside the Commission's jurisdiction because, for instance, they are state-owned, *see* 16 U.S.C. § 824(f)—would otherwise not have to offer open-access. Under the Tariff, a public utility does not have to offer them access unless they reciprocate. In order to avoid controversies between public and non-public utilities regarding reciprocal service, the

Commission adopted a voluntary "safe harbor" provision pursuant to which non-public utilities could submit a transmission tariff to the Commission for a (36)determination whether it satisfied the reciprocity condition. If it did, the public utility would have to offer service; if it did not, the public utility could refuse service (although it had the option of waiving the reciprocity condition, as did the Commission itself).

A. *Indirect Regulation of Non-Jurisdictional Utilities*

Nebraska Public Power District (NPPD), a state entity, provides electrical generation, transmission and distribution service to wholesale and retail customers throughout Nebraska.[7] It claims that the Commission, through the reciprocity provision, has reached beyond its statutory authority and is illegally attempting to regulate entities, including NPPD, over which the Commission has no jurisdiction, in violation of the Federal Power Act and the Tenth Amendment to the Constitution. NPPD admits that pursuant to Nebraska law, all state power districts are obligated to provide open access transmission service. They have been doing so for years. This is doubtless why, after Order No. 888 issued, another Nebraska public power district so easily obtained a safe harbor declaration. *See Omaha Pub. Power Dist.*, 81 F.E.R.C. ¶ 61,054 (1997). In light of this, the Commission argues—and we agree—that NPPD's petition is unripe. Since NPPD already offers open access transmission, it is far from certain that the reciprocity provision will have any effect on it.[8] It certainly has not demonstrated any particular hardship that it

---

[7] "Nebraska is unique among the States in the Union in that *all* generation, transmission and distribution service is provided by public entities, municipalities and cooperatives whose governing boards are responsible to, and serve at the voting pleasure of, the rate-payers they serve." NPPD Brief at 2.

[8] The Commission made clear that existing contracts will not be affected. *See* Order 888-A, ¶ 31,048 at 30,181.

would suffer if we refused to engage in pre-enforcement judicial review. *See AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 386 (1999). From all that appears, no public utility has refused, or even threatened to refuse, to give NPPD access to its transmission system in the wake of (37)Order No. 888.[9] Given the fact that public utilities may waive the reciprocity provision anyway, and that NPPD has the same option of obtaining a safe harbor as did the Omaha Public Power District, we are not persuaded that the provision is currently altering NPPD's conduct of its affairs or that withholding judicial review will cause it any hardship whatever. "Unlike the drug manufacturers in *Abbott Laboratories [v. Gardner*, 387 U.S. 136 (1967)], but like the cosmetics companies in *Toilet Goods Ass'n v. Gardner*, 387 U.S." 158, 164 (1967), NPPD need not change its "behavior or risk costly sanctions." *Clean Air Implementation Project v. EPA*, 150 F.3d 1200, 1205 (D.C. Cir. 1998). Furthermore, exactly how the Commission will fill in the contours of the reciprocity provision remains to be seen. That it may defer to state commissions, as it indicated in *Houston Lighting & Power Co.*, 81 F.E.R.C. ¶ 61,015 (1997), *order on reh'g*, 83 F.E.R.C. ¶61,181 (1998), affects NPPD's contention that the Commission is seeking to bring about nationwide uniformity by forcing non-public utilities to comply with its "detailed mandates." NPPD Brief at 5. We therefore believe the issues raised would benefit from a more concrete setting in which NPPD can demonstrate exactly how the reciprocity provision has affected its primary conduct. *See Clean Air Implementation Project*, 150 F.3d at 1204. For all these reasons, NPPD's challenge to the reciprocity provision is not ripe for judicial review.

---

[9] For this reason we find unpersuasive NPPD's claim that the Tariff's reciprocity provision places it at a disadvantage in negotiations because a public utility may simply refuse to provide service without any fear of a Commission enforcement action. *See* NPPD Reply Brief at 4-5.

B. *Limitation on Reciprocity*

The Investor Owned Utilities (IOUs) challenge the following limitation on reciprocity: non-public utilities owe reciprocal open access only to the public utility from which they take open access service—not to all utilities. *See* IOU Brief at 40-44; IOU Reply Brief at 18-20. These petitioners argue that the Commission has left open the door for non-public utilities (38)to discriminate against all other utilities and that it has done so solely because of tax considerations that no longer apply.

We agree with Commission counsel that tax considerations were not the only basis on which the Commission's limitation rested. The Commission stated that "the reciprocity requirement strikes an appropriate balance by limiting its application to circumstances in which the non-public utility seeks to take advantage of open access on a public utility's system." Order 888, ¶ 31,036 at 31,762. The Commission also explained that it "do[es] not have the authority to require non-public utilities to make their systems generally available." *Id.* at 31,761. The Commission stated also that it did not want broad open access reciprocity to jeopardize the tax-exempt financing non-public utilities enjoy,[10] that the IRS was then reexamining the question, *id.* at 31,762, and that if the tax issue is favorably resolved, it will reconsider the matter. Order 888-A, ¶ 31,048 at 30.287. The IRS has now acted. *See* Temporary Regulations § 1.141-7T(f), *in* 63 Fed. Reg. 3256 (1998). The IOUs argue that we must therefore remand for reconsideration. *See* IOU Brief at 44 (citing *Panhandle Eastern Pipeline v. FERC*, 890 F.2d 435, 439 (D.C. Cir. 1989); *National Fuel Gas Supply Corp. v. FERC*, 899 F.2d 1244, 1249-50 (D.C. Cir. 1990); *Ciba-Geigy v. EPA*, 46 F.3d 1208 (D.C. Cir. 1995)).

---

[10] *See* 26 U.S.C. §§ 141, 142 (permitting "private activity" bonds and "local furnishing" bonds, respectively).

We think not. So far as we know, the IRS has not finalized its temporary and proposed regulations. The IRS acknowledges that its temporary regulations "raised[ ] a number of complex technical issues" many of which "may need to be addressed legislatively" and it anticipates that the finalization process will take three years to accomplish. 63 Fed. Reg. at 3258-59. Second, as the Commission indicates, the possible tax consequences of requiring open access from non-jurisdictional utilities was its secondary concern. The Commission's greater concern was its lack of jurisdiction to do what the IOUs ask. And lastly the Commission should be (39)taken at its word that it will reconsider the scope of reciprocity when and if the temporary tax regulations are finalized.

V. STRANDED COST RECOVERY PROVISIONS

Ordering open access transmission, Order 888-A explains that "[t]he most critical transition issue that arises as a result of the Commission's actions in this rulemaking is how to deal with the uneconomic sunk costs that utilities prudently incurred under an industry regime that rested on a regulatory framework and a set of expectations that are being fundamentally altered." Order 888-A, ¶ 31,048 at 30,346. "If a former wholesale requirements customer or a former retail customer uses the new open access to reach a new supplier," FERC said, "we believe that the utility is entitled to recover legitimate, prudent and verifiable costs that it incurred under the prior regulatory regime...." Order 888, ¶ 31,036 at 31,789.

According to FERC, these "stranded" costs consist predominantly of costs of building generation capacity, which utilities incurred with the expectation that they would use the additional capacity to serve existing customers. *See* Notice of Proposed Rulemaking, *Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, FERC Stats. & Regs.

¶ 32,507 at 32,863-64, 59 Fed. Reg. 35,274 (1994) ("Stranded Cost NOPR"). Because of the increased competition in the generation market that will result from open access, this capacity may become underutilized or uneconomical, *i.e.*, "stranded." Stranded costs also include nonrecurring costs approved by regulators that, in order to avoid rate increases, were recovered over a period of years instead of at the time the expenditures were made. Known as "regulatory assets," these costs include deferred income taxes, deferred pension and other employee benefit and retirement costs, research and development, extraordinary property losses, and the phase-in of new plant costs. Nuclear decommissioning costs and costs to buy out high-priced fuel and power contracts may also become stranded as a result of open access.

(40)Exercising its exclusive jurisdiction over wholesale power sales, FERC through Order 888 gave utilities the opportunity to recover their stranded costs from former wholesale customers who take advantage of open access transmission to purchase power from other suppliers. Order 888, ¶ 31,036 at 31,810. With respect to stranded costs resulting from state-ordered retail wheeling, Order 888 provides that FERC will consider stranded cost claims only when state regulatory agencies lack authority to do so. *Id.* at 31,824-25. Order 888 also designated FERC as the primary forum for stranded cost claims stemming from what are known as new municipalizations and municipal annexations. *See* Order 888-A, ¶ 31,048 at 30,404; Order 888-B, 81 FERC at 62,104. Stranded costs in these situations result from retail (as opposed to wholesale) power sales.

Petitioners challenge nearly every aspect of FERC's stranded cost policy as set forth in Order 888, from the mechanics of calculating customers' stranded cost obligations to whether FERC has authority to address stranded costs at all. We begin with those challenges that relate to the recovery of wholesale stranded costs (Section V.A), then turn to challenges to Order

888's treatment of retail stranded costs (Section V.B). We affirm FERC's stranded cost policy in all respects, except we vacate that portion of the orders dealing with the treatment of energy costs in the market option and remand to FERC for further explanation. *See* Section V.A.5.c.

A. *Wholesale Stranded Costs*

In requiring nondiscriminatory open access transmission as a remedy for undue discrimination, FERC recognized that it "cannot change the rules of the game without providing a mechanism for recovery of the costs caused by such regulatory-mandated change." Order 888-A, ¶ 31,048 at 30,346. Under the pre-open access regulatory regime, utilities entered into long-term contracts to make wholesale power sales to municipal, cooperative, and investor-owned utilities. *See* Stranded Cost NOPR, ¶ 32,507 at 32,862. Because these customers had no source of power supply other than (41)their historic utility, these contracts were typically extended at the end of their term. This produced an implicit obligation by the utilities to continue satisfying their customers' power needs, as well as a reciprocal expectation by customers of continued service. *See id.* at 32,863-64. To satisfy expected customer demand, utilities invested money, built facilities, and entered into long-term fuel or power contracts, relying on the "regulatory compact" under which utility shareholders accepted lower rates of return on their investment in exchange for the certainty of regulated rates and resulting ability to recover prudently incurred costs. *See* Notice of Proposed Rulemaking, *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, FERC Stats. & Regs. ¶ 32,514 at 33,049, 60 Fed. Reg. 17,662 (1995).

Order 888 fundamentally undermines utilities' expectation of continued service and cost recovery. A utility's requirements

customers may now use the utility's open access transmission service to purchase power from other suppliers at the end of their contract terms. If customers leave before paying their share of costs the historic utility incurred on their behalf, the utility will be left with stranded costs, which it will either absorb or shift to remaining customers.

Unless utilities are able to recover stranded costs, FERC reasoned, their ability to compete and attract investor capital in a deregulated market may be seriously impaired. FERC therefore decided that it had to "address recovery of the transition costs of moving from a monopoly-regulated regime to one in which all sellers can compete on a fair basis and in which electricity is more competitively priced." Order 888, ¶ 31,036 at 31,635. In reaching this conclusion, FERC relied on its experience in restructuring the natural gas industry, where this court faulted it for failing to provide transitional mechanisms such as stranded cost recover. FERC explained: "We have learned from our experience in the natural gas area the importance of addressing competitive transition issues early and with as much certainty to market participants as possible." *Id.*

(42)In shaping its stranded cost recovery mechanism, FERC had to balance two competing interests: speeding the transition to competition versus protecting utilities that had incurred costs with the expectation that their customers would remain and eventually pay those costs through electricity rates. Allowing recovery of stranded costs, FERC acknowledged, would delay full realization of the benefits of open access—lower electricity rates—because customers facing stranded cost liability might continue purchasing power from their historic utility even though competitors are selling power at lower rates. *See* Order 888-A, ¶ 31,048 at 30,355. Indeed, a customer would only switch suppliers if the competitor offered a rate less than the historic utility's rate plus the customer's stranded cost liability. But given the highly regulated nature of the electricity industry, in which

utilities incurred costs with the expectation of recouping them, FERC concluded that the delay was a necessary component of its open access program. *See id.* Mindful of its ultimate goal of converting the electricity industry into a competitive market, however, FERC fashioned the stranded cost recovery provisions to be transitional, allowing utilities to recover stranded costs only in connection with wholesale requirements contracts entered into on or before July 11, 1994 (the date of the stranded cost notice of proposed rulemaking). *See* 18 C.F.R. § 35.26(b)(8), 35.26(c)(1)(v)-(vi).

As to precisely who should pay for stranded costs, utilities and customers not surprisingly had dramatically different positions. Customers argued that utilities should absorb most, if not all, stranded costs. Utilities (and their investors) argued that customers should pay.

Facing an enormously difficult task in balancing these sharply conflicting positions, FERC crafted a rule that requires customers to pay stranded costs but only in certain circumstances. Most important, in order to recover stranded costs from a customer, the historic utility must prove that it had a reasonable expectation of continued service to that particular customer for a certain number of years beyond the end of the contract term; a utility unable to prove such an expectation may not recover stranded costs under Order 888. (43)*See* 18 C.F.R. § 35.26(c)(2)(i). Moreover, a utility able to demonstrate a reasonable expectation of continued service may recover stranded costs only if its wholesale customer actually takes advantage of the utility's open access tariff to obtain access to a new generation supplier at the end of its contract term (*i.e.*, the former customer continues to use the historic utility's transmission service but no longer purchases power from it). *See* 18 C.F.R. § 35,26(b)(1)(i). Through these two limitations, FERC balanced the interests of utilities and customers by allowing utilities to recover their stranded costs only if they can

demonstrate a reasonable expectation of continued service and requiring customers to pay those costs only if they take advantage of their historic utility's open access transmission to reach cheaper sources of power. And of course, no customer will have to pay stranded costs at all if it continues purchasing power from its historic utility throughout the period during which the utility has a reasonable expectation of continued service —precisely what the customer would have done in the absence of Order 888's open access requirement.

Under Order 888, stranded costs are calculated on a "revenues lost" basis. A departing customer's stranded cost obligation equals the estimated revenue it would have paid had it continued to purchase power from the historic utility minus the current market value of the power it would have purchased, calculated over the period the utility is determined to have a reasonable expectation of continued service to that customer. *See* 18 C.F.R. § 35.26(c)(2)(iii). In other words, the stranded cost formula is not tied to particular stranded assets or contractual commitments, but rather awards utilities the difference between the pre-open access cost-based rate and the post-open access market rate. Once a customer's stranded cost liability is calculated, it may pay through a lump-sum payment, installment payments, or a surcharge to the transmission rate charged by the historic utility. *See* Order 888, ¶ 31,036 at 31,799.

Before turning to petitioners' arguments, we emphasize what should be obvious from the foregoing summary of Order 888: Order 888 awards stranded costs to no one. It does (44)nothing more than establish a mechanism by which utilities may seek to recover stranded costs. To recover stranded costs, a utility must demonstrate its continued expectation of service at an evidentiary hearing. The customer may appear at that hearing and, through evidentiary submissions of its own, attempt to demonstrate that the utility had no such expectation. Only after

such a hearing may FERC decide whether a utility can recover stranded costs and, if so, how much.

Petitioners mount many challenges to Order 888's stranded cost recovery provisions. For purposes of analysis, we group these challenges into five categories: (1) challenges to FERC's authority to provide for stranded cost recovery (section V.A.1); (2) claims that Order 888 conflicts with cost causation principles and case law developed under the Natural Gas Act (section V.A.2); (3) challenges to FERC's *Mobile-Sierra* findings (section V.A.3); (4) claims that FERC arbitrarily and capriciously failed to provide for stranded cost recovery by certain entities, such as transmission dependent utilities and generation and transmission cooperatives (section V.A.4); and (5) challenges to various technical aspects of Order 888's stranded cost recovery provisions (section V.A.5).

1. *FERC's Authority to Provide for Stranded Cost Recovery*

A group called Petitioners Opposing Stranded Cost Recovery ("POSCR") advances three challenges to FERC's authority to provide for stranded cost recovery: (1) as a factual matter, utilities could nver have had a reasonable expectation of continued service to wholesale customers beyond the contract term; (2) sections 206 and 212 of the Federal Power Act ("FPA") forbid stranded cost recovery; and (3) our decision in *Cajun Elec. Power Coop., Inc. v. FERC*, 28 F.3d 173 (D.C. Cir. 1994), holds that stranded cost recovery is anticompetitive. We consider each argument in turn.

a. *Reasonable expectation of continued service*

To recover stranded costs relating to a specific departing wholesale requirements customer, a utility must show that it (45)had a reasonable expectation of service to that customer beyond the term of its existing contract. *See* 18 C.F.R. §

35.26(c)(2)(i). Pointing out that contracts define the extent of the parties' obligations and that customers have long exercised their rights to purchase power from other suppliers at the end of their contract terms, POSCR contends that utilities could never have had an expectation of service beyond their contract terms. In considering this argument it is important to remember that Order 888 does not itself award stranded costs; it merely establishes a procedure by which utilities may petition FERC in individual proceedings to recover stranded costs from a specific customer based on a specific evidentiary showing. Utilities failing to show an expectation of continued service will be unable to recover stranded costs. POSCR's challenge thus amounts to a claim that no utility could ever, under any circumstances, have had a reasonable expectation to serve a wholesale customer beyond the term of its contract. We review this claim under the APA's familiar arbitrary and capricious standard. *See* 5 U.S.C. § 706(2)(A); *Williams Field Services Group, Inc. v. FERC*, 194 F.3d 110, 115 (D.C. Cir. 1999).

Responding to this same challenge in Order 888-A, FERC explained that utilities historically had an implicit obligation to serve customers beyond the contract term for a simple reason: Customers had no means of reaching alternative suppliers. *See* Order 888-A, ¶ 31,048 at 30,354. As part of that obligation to serve, FERC found, a local utility "had a concomitant obligation to plan to supply [its] customers' continuing needs, and planned its system taking account of the wholesale load. In many cases the wholesale customers participated by supplying load forecasts." *Id.* In making capital decisions and predicting future demand, utilities frequently consulted with their wholesale requirements customers. For these reasons, FERC concluded, utilities may have a reasonable expectation of continued service to particular customers. *See id.* at 30,354-55.

Not only is FERC's judgment about utilities' reasonable expectations precisely the type of policy assessment to which we

owe great deference, but POSCR points to nothing sug-(46)gesting that FERC's reasoning is arbitrary and capricious. In fact, POSCR's argument completely ignores the highly regulated nature of the electricity industry prior to Order 888. Unlike competitive markets, where buyers may freely purchase from many sellers, the monopolistic character of the electricity industry, combined with the congressionally imposed regulatory structure, left requirements customers highly dependent on a single supplier—their historic utility. Indeed, as interveners point out, utilities were even unable to choose not to renew an expiring wholesale requirements contract without first notifying FERC. *See* 18 C.F.R. § 35.15 (1995) (repealed by Order 888). Although it may well be true, as POSCR argues, that some wholesale customers have long been able to purchase unbundled transmission service, we think such evidence is best reserved for individual proceedings, where a department customer can attempt to refute the utility's claim that it had an expectation of continued service.

b. *Sections 206 and 212 of the FPA*

Section 206(a) of the FPA gives FERC authority to "determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force" if it finds that any existing arrangement "is unjust, unreasonable, unduly discriminatory or preferential." 16 U.S.C. § 824e(a). Relying on section 206(a) as the basis for Order 888, FERC found that utilities had used their monopoly transmission power to discriminate against potential competitors and that such practices would increase as competitive pressures in the industry increased. Order 888, ¶ 31,036 at 31,676, 31,682.

POSCR contends that Order 888's stranded cost recovery provisions themselves violate FERC's own construction of section 206, the construction FERC relied on as the basis for the open access rule. According to POSCR, "[t]he stranded cost rule

perpetuates the very 'discrimination' FERC found unlawful, and subjects the same victims—customers held hostage to uneconomic electric generation by transmission monopolists—to continued abuse."

(47)In challenging FERC's policy decision to provide for stranded cost recovery, POSCR conflates the violation (FERC's generic determination that utilities' practice of prohibiting access to their transmission lines on reasonable terms was unduly discriminatory) with the remedy (FERC's more limited finding that recovery of stranded costs in particular circumstances would not be unduly discriminatory). FERC has not, as POSCR contends, given "unduly discriminatory" different meanings; rather, it has applied the term in different contexts.

POSCR's argument thus boils down to a challenge to FERC's conclusion that the stranded cost recovery prescribed in Order 888 is not unduly discriminatory, a challenge meriting arbitrary and capricious review. Viewed through this lens, we think FERC more than adequately explained why it concluded that stranded cost recovery is not unduly discriminatory—stranded cost recovery, FERC said, is transitional only, follows cost causation principles, and requires utilities to prove that they had a reasonable expectation of continued service. FERC faced an enormously difficult task. It had to balance the transition to competitive markets against the need to maintain the competitiveness of utilities that had incurred costs based on a reasonable expectation that they would recoup them. We find nothing either arbitrary or capricious in how FERC struck this balance.

POSCR next contends that stranded cost recovery violates section 212 of the FPA, which governs the rates for transmission ordered by FERC pursuant to section 211. 16 U.S.C. §§ 824j-k. Because FERC-jurisdictional utilities are no longer subject to sections 211 and 212, this argument relates only to those

situations in which FERC orders nonjurisdictional transmitting utilities to wheel under section 211 and these utilities then seek to recover stranded costs in their transmission rates. *See* 18 C.F.R. § 35.26(c)(1)(vi)-(vii). Section 212 allows FERC to order "rates, charges, terms, and conditions which permit the recovery by [a transmitting] utility of all the costs incurred in connection with the transmission services and necessary associated services, including, but not limited to, an appropriate share, if any, of legitimate, verifiable and (48)economic costs, including taking into account any benefits to the transmission system of providing the transmission service, and the costs of any enlargement of transmission facilities." 16 U.S.C. § 824k(a). Contending that "economic costs" cannot be read to include payment of stranded costs, which by definition relate to generation (not transmission) services, POSCR reads section 212 to preclude stranded cost recovery.

Straightforward application of the *Chevron* doctrine demonstrates the lack of merit in this argument. *See Chevron, U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984). Because Congress has not "directly spoken to the precise question at issue"—do "economic costs" include stranded costs?—and because nothing in the statute precludes recovering through transmission rates costs that were traditionally recovered through generation rates, the term "economic costs" is ambiguous. *Id.* at 842.

Proceeding to *Chevron*'s second step, we ask whether FERC has reasonably interpreted the term "economic costs." *See id.* at 843. We have no doubt that it has. As FERC explained, but for section 211 wheeling orders, there would be no stranded costs. Stranded costs, according to FERC, are therefore economic costs of section 211 wheeling. *See* Order 888-A, ¶ 31,048 at 30,390. POSCR offers nothing to undermine this eminently reasonable interpretation of the statute.

c. *Implications of* Cajun

Next, POSCR contends that our decision in *Cajun Elec. Power Coop., Inc. v. FERC*, 28 F.3d 173 (D.C. Cir. 1994), condemns stranded cost recovery as anticompetitive. A pre-Order 888 decision, *Cajun* reviewed two tariffs allowing a utility, Entergy Corporation, to sell power at market rates, and a third tariff providing for open access to Entergy's transmission services at cost-based rates. The third tariff gave Entergy an opportunity to recover stranded costs from customers who no longer purchase power from Entergy but use its transmission lines to reach other suppliers—exactly the circumstances in which Order 888 provides for stranded cost recovery. Under the tariff, the stranded cost charge was included in Entergy's transmission rate. *See id.* at 175-77.

(49)Characterizing the stranded cost provision as a "tying arrangement" under antitrust law, *Cajun* explained that under the tariff, Entergy could charge a former customer for the cost of generation services when the customer wished to purchase only transmission services; because Entergy has a monopoly over transmission, customers would have no choice but to pay costs relating to generation they no longer wanted from Entergy. *Id.* at 177-78. Thus, because "Entergy could use its monopoly over transmission services to eliminate competition in the market for generation services," the net effect of the tariffs may be anticompetitive. *Id.* at 176.

Of significance to this case, however, we did not strike down the tariffs. Instead, we remanded the case for FERC to determine "how much competition in fact is dampened" by the stranded cost provision. *Id.* at 178. Thus, contrary to POSCR's suggestion, *Cajun* does not represent a blanket condemnation of stranded cost recovery; rather, recognizing that such recovery could be anticompetitive, *Cajun* directed FERC to evaluate and justify the potential anticompetitive impact. This is precisely

what FERC has done in Order 888. It expressly considered the anticompetitive effects of stranded cost recovery. *See* Order 888-A, ¶ 31,048 at 30,372-74. Then, stressing the transitional nature of the recovery and the fact that recovery was compelled by the open access requirement, which utilities could not have anticipated, FERC concluded that the limited anticompetitive effects of stranded cost recovery were both a necessary and acceptable consequence of the transition to competition. *See id.* Not only has POSCR offered no evidence that would lead us to question FERC's conclusion, but such judgments about anticompetitive effects are "the kind of reasonable agency prediction about the future impact of its own regulatory policies to which we ordinarily defer." *Louisiana Energy and Power Auth. v. FERC*, 141 F.3d 364, 370 (D.C. Cir. 1998).

2. *Natural Gas Precedent and Conformance to Cost Causation Principles*

Having rejected POSCR's arguments that FERC lacks authority to authorize stranded cost recovery, we turn to its (50)argument that FERC has failed adequately to explain why Order 888 requires departing customers to pay one-hundred percent of stranded costs. In support of this argument, POSCR claims that our decisions reviewing FERC's restructuring of the natural gas industry require cost sharing; it also argues that Order 888's stranded cost recovery conflicts with the cost causation principles that traditionally govern allocation of costs.

a. *Natural gas precedent:* AGD, K N Energy, *and* UDC

In introducing competition into the electricity industry, FERC has taken essentially the same path that it took in restructuring the natural gas industry, although what FERC has done in a single order in the electricity industry (Order 888) it did in a series of orders in the natural gas industry. Because POSCR

relies so heavily on FERC's natural gas orders and our decisions reviewing them, we begin by summarizing them in some detail.

Finding practices in the natural gas industry "unduly discriminatory" in violation of the Natural Gas Act, FERC began by issuing Order 436, which "unbundled" pipeline transportation and merchant functions. *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol,* Order No. 436, FERC Stats. & Regs. ¶ 30,665, 50 Fed. Reg. 42,408 (1985) (rehearing orders omitted). At the time of Order 436, pipelines were facing enormous liabilities under long-term "take-or-pay" contracts. Entered into when gas prices were expected to rise, these contracts obligated pipelines to purchase minimum quantities of gas from wellhead producers at fixed prices that turned out to be well in excess of market prices. *See Associated Gas Distributors v. FERC*, 824 F.2d 981, 1021 (D.C. Cir. 1987) ("*AGD*"). Although FERC estimated take-or-pay liabilities at billions of dollars, and although Order 436 would exacerbate the take-or-pay problem by providing incentives to pipeline customers to purchase gas from cheaper suppliers, FERC declined to take any action with respect to the contracts. In *AGD*, we found that FERC's decision to do nothing failed to meet the requirements of reasoned decisionmaking, citing FERC's "seeming (51)blindness to the possible impact of Order No.436 on take-or-pay liability" and permanent market distortions that may result from FERC's inaction. *Id.* at 1021-23, 1025. Specifically, we noted, in words echoed by FERC years later in Order 888, that consumers who purchased from the "least nimble" local distribution companies would "be stuck with the burden of the overpriced gas." *Id.* at 1023.

In response to *AGD*, FERC issued Order 500. *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 500, FERC Stats. & Regs. ¶ 30,761, 52 Fed. Reg. 30,334 (1987) (rehearing orders omitted). Recognizing that no one segment of the gas industry was wholly responsible for the take-

or-pay problem, Order 500 allowed pipelines to recover take-or-pay costs through "equitable sharing." Pipelines that willingly absorbed twenty-five to fifty percent of their costs could require sales customers to match that amount through a fixed charge. Pipelines could recover any balance through commodity rates or volumetric surcharges, borne by both sales and transportation customers. For an overview of these components of Order 500, see *K N Energy, Inc. v. FERC*, 968 F.2d 1295, 1297-98 (D.C. Cir. 1992). We sustained this approach in *K N Energy*, holding that even though Order 500 replaced traditional "cost causation" principles with cost spreading and value-of-service concepts, it did not violate Natural Gas Act section 4's requirement that rates be just and reasonable. *Id.* at 1301-02. Citing statements in *AGD* that "all actors in the natural gas industry" are "candidates" for absorbing take-or-pay liability, we relied on "the unusual circumstances surrounding the take-or-pay problem, and the limited nature—both in time and scope—of the Commission's departure from the cost-causation principle." *Id.* at 1301.

Concluding that Order 436 had been only partially successful in introducing competition into the natural gas industry, FERC issued its third major restructuring order, Order 636. *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, FERC Stats. & Regs. ¶ 30,939, 57 Fed. (52) Reg. 13,267 (1992) (rehearing orders omitted). That order imposed mandatory unbundling of sales and transportation services and allowed sales customers to reduce the amount of gas they had to purchase pursuant to existing contracts. When customers took advantage of this option and purchased gas from sources other than the pipelines, the pipelines were once again left with substantial take-or-pay liabilities. Labeling the costs of reducing these liabilities gas supply realignment or GSR costs, Order 636 authorized pipelines to bill current transportation customers for one-hundred percent of their GSR costs by charging either a

negotiated exit fee or reservation fee surcharge. Order 636 also authorized pipelines to recover all stranded costs in rate filings. In the natural gas industry, stranded costs represented the costs of pipeline assets (such as storage facilities) used to provide bundled sales services that were not directly assignable to transportation customers. For an overview of these components of Order 636, see *United Distribution Cos. v. FERC*, 88 F.3d 1105, 1125-27, 1176-78 (D.C. Cir. 1996) ("*UDC*").

In *UDC*, we affirmed FERC's determination that pipelines could recover all stranded costs through filed rates, so long as FERC "adequately balanced the interests of investors and ratepayers." *Id.* at 1180. Reaffirming the appropriateness of the cost spreading and value-of-service principles approved in *K N Energy*, we found that FERC's allocation of GSR costs to pipeline transportation customers, as opposed to the pipelines themselves, properly applied those principles. *Id.* at 1182. Although recognizing that GSR costs stemmed from pipeline sales customers, not transportation customers, we found that FERC appropriately imposed the costs on transportation customers because these customers benefitted from the availability of lower-priced transportation and also because FERC could not spread costs to the pre-Order 636 sales customers since those customers no longer purchased gas from the pipelines. *Id.* at 1185-86. We remanded for FERC to explain more fully why pipelines should not have to pay some of the costs, noting an inconsistency in the Commission's analysis: While FERC applied *cost spreading* principles to justify imposing costs on transportation customers, it (53)invoked *cost causation* principles in concluding that pipelines should not have to pay any of these costs. *Id.* at 1188-90. We explicitly stated, however, that we were not saying that "it is impossible, or even improbable, that the Commission on remand can establish a convincing rationale for exempting the pipelines." *Id.* at 1189.

POSCR reads this history to require FERC to order cost sharing, but it ignores Order 888's explanation of the difference between natural gas restructuring and the situation in the electricity industry. Most fundamentally, Order 888 explains, stranded cost recovery in the electricity industry conforms to cost causation principles, which normally govern the allocation of costs and require customers to pay the costs they caused. *See* Order 888, ¶ 31,036 at 31,798. Cost causation principles could not be applied in natural gas restructuring, Order 888 explains, because many customers had already begun purchasing gas from other suppliers before FERC had addressed the take-or-pay problem on remand from *AGD*, and because the filed rate doctrine prohibits assessing charges against former customers. *Id.* at 31,800-01. Order 888 also explains that unlike stranded costs in the electricity industry, the take-or-pay liabilities in the gas industry were extraordinary. The billions of dollars of take-or-pay liabilities resulted not from Order 636, but from earlier regulatory policies that had encouraged pipelines to enter into long-term, fixed-price gas purchase contracts, combined with declining gas prices that made those contracts uneconomical. *See* Order 888-A, ¶ 31,048 at 30,380. Under all of these circumstances, "[t]o have allocated these costs solely to any one segment of the industry would have imposed a crushing new burden on that segment." *Id.* at 30,380-81.

Stranded costs in the electricity industry, Order 888 explains, are quite different. Resulting directly from Order 888, they represent "ordinary costs that have always been, and are currently, included in the utility's rates for electric generation approved by the Commission." *Id.* at 30,382. Moreover, wholesale customers may avoid stranded cost liability by continuing to purchase power from their historic utility, precisely what they probably would have done in the (54)absence of Order 888. In other words, in contrast to the natural gas industry, where customers would have faced enormous new burdens had FERC forced them to pay take-or-pay costs, customers in the

electricity industry face no new burdens; instead, Order 888 requires them to pay nothing more than costs they would have had to pay in the absence of Order 888. In the electricity industry, the only effect of stranded cost recovery is delayed realization of the full benefits of a competitive market.

In light of these differences between the natural gas and electricity industries and FERC's exhaustive treatment of the natural gas restructuring in Order 888, POSCR's contention that FERC has failed "to offer a coherent rationale, rising to the level of reasoned decisionmaking" for not imposing cost sharing is wholly without merit. Equally without merit is POSCR's assertion that *UDC* "teaches that, were customers and utilities benefit from an open access rule/order that leads to early contract termination and where anticompetitive conduct by utilities has given rise to the need for the open access order, utilities must share transition costs." POSCR ignores three important points. First, FERC, not this court, determined that cost sharing was appropriate with respect to take-or-pay liabilities. *UDC* merely affirmed FERC's decision. Second, *K N Energy* recognized that cost sharing in the natural gas industry was a departure from the cost causation principles that normally apply, a departure justified by extraordinary circumstances in the natural gas industry. *K N Energy*, 968 F.2d at 1301-02. And finally, as to stranded costs that more closely resemble those at issue in this case—for example, pipeline assets that would no longer be fully employed when customers took advantage of unbundling to purchase gas from alternative suppliers—FERC ordered, and *UDC* affirmed, that pipelines recover one-hundred percent of those costs.

b. *Conformance to cost causation principles*

Having established that the natural gas cases impose no obligation on FERC to order cost sharing, we next consider POSCR's argument that the inclusion of stranded costs in

(55)transmission rates does not conform to cost causation principles. This is so, POSCR asserts, because Order 888's stranded cost provisions require customers to pay through transmission rates for costs the utility previously incurred to provide generation services.

As an initial matter, we note that payment through transmission rates is only one of three ways that a departing customer may pay its stranded cost obligation; the customer also has the option of making a lump-sum payment or installment payments. Thus POSCR's challenge seems aimed only at the method of payment, not at the fact that payment is required. But even viewing POSCR's challenge more broadly, as a claim that stranded cost recovery no matter what the method of payment violates cost causation principles, we think it lacks merit.

We have explained the cost causation principle as follows: "Simply put, it has been traditionally required that all approved rates reflect to some degree the costs actually caused by the customer who must pay them." *K N Energy*, 968 F.2d at 1300. Given this definition, we are puzzled by POSCR's claim that because inclusion of stranded costs in transmission rates requires customers to pay currently for costs incurred in the past, it violates cost causation principles. To some degree, all utility rates reflect past costs; utilities typically expend funds today (for example, constructing generation facilities), fully expecting to recover those costs through future rates. In fact, current rates often include past costs that utilities deferred in order to avoid rate increases. Cost causation requires not that costs be incurred at the same time they are included in rates, but that the rates "reflect to some degree the costs actually caused by the customer who must pay them." *Id.*

In fashioning Order 888's stranded cost recovery provisions, FERC went to great lengths to ensure that customers would be responsible for only those costs they caused.

> [T]he Rule is consistent with the traditional cost causation principle because it recognizes the link between the incurrence of the stranded costs and the decision of a (56)particular generation customer to use open-access transmission on the utility's system to leave the utility's generation system and shop for power, and bases the utility's ability to recover stranded costs on its ability to demonstrate that it incurred costs with the reasonable expectation that the customer would remain on its generation system beyond the term of the contract.

Order 888-A, ¶ 31,048 at 30,382.

We cannot see how including stranded costs in transmission rates instead of lump sum payments changes this analysis. To the extent POSCR is arguing that including in a transmission rate costs incurred to provide generation services violates cost causation principles, we reiterate that stranded costs are not costs of providing the physical transmission services but, as Order 888-A explains, they are utilities' cost of open access transmission. *See* Order 888-A, ¶ 31,048 at 30,389 & n.634. More generally, given the fundamental changes wrought by Order 888 and the unprecedented opportunity for customers to purchase power from alternative suppliers, we are quite comfortable deferring to FERC's judgment that stranded cost recovery—through transmission rates or otherwise—conforms to cost causation principles. In fact, FERC may have violated cost causation principles had it failed to assign stranded costs to customers who caused them.

POSCR next argues that Order 888 is unduly discriminatory because including stranded costs in transmission rates forces transmission customers who previously used a utility's generation capacity to pay higher costs than new transmission customers.

Disagreeing, FERC determined that requiring customers receiving similar services to pay different rates is necessitated by Order 888's open access requirement. *See* Order 888-A, ¶31,048 at 30,388-90. *Cf. AGD*, 824 F.2d at 1009 ("[T]he mere fact of a rate disparity is not enough to constitute unlawful discrimination.") (internal quotation marks omitted). Moreover, FERC concluded, the application of cost causation principles justifies this different treatment. *See* Order 888-A, ¶ 31,048 at 30,379, 30-388-90. Seeing noth-(57)ing unreasonable (let alone arbitrary or capricious) in FERC's policy judgment, we reject POSCR's challenge.

Nor do we agree with POSCR's argument that stranded cost recovery violates the filed rate doctrine, which "forbids a regulated entity to charge rates for its services other than those properly filed with the appropriate federal regulatory authority." *Western Resources, Inc. v. FERC*, 72 F.3d 147, 149 (D.C. Cir. 1995). In *Western Resources*, we held that FERC's assignment to current customers of costs relating to take-or-pay liabilities did not violate the filed rate doctrine. Recognizing that "a central purpose of the doctrine is to enable purchasers to know in advance the consequences of the purchasing decisions they make," we determined that the doctrine was satisfied where customers received "adequate notice of a rate in advance of the service to which it relates." *Id.* at 149-50 (internal quotation marks omitted). Order 888's stranded cost policy satisfies this requirement because customers electing to purchase power generation from a source other than the transmitting utility from which they had purchased power in the past will be aware of the costs when making that decision.

3. *FERC's* Mobile-Sierra *Findings*

Under the Supreme Court's *Mobile-Sierra* doctrine, where parties have negotiated a contract that sets firm prices or dictates a specific method of computing charges and includes a clause

denying either party the right to change such prices or charges unilaterally, "FERC may abrogate or modify the contract only if the public interest so requires." *Texaco, Inc. v. FERC*, 148 F.3d 1091, 1095 (D.C. Cir. 1998); *see also FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 353-55 (1956); *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344-45 (1956). We have recognized that "the 'public interest' that permits FERC to modify private contracts is different from and more exacting than the 'public interest' that FERC seeks to serve when it promulgates its rules." *Texaco*, 148 F.3d at 1097.

FERC usually makes *Mobile-Sierra* determinations on a case-by-case basis. A party seeking to modify a contract (58)containing a *Mobile-Sierra* clause petitions FERC. That party bears the burden of convincing FERC that the modification is in the public interest.

Order 888 departs from this normal case-by-case practice by making two generic public interest findings, one focused on utilities, the other on customers. These generic findings relieve utilities and customers of the burden of demonstrating in individual proceedings that the proposed modifications are in the public interest. As to utilities, Order 888 ruled that it was in the public interest to allow them to add stranded cost amendments to their contracts if they could demonstrate, in accordance with Order 888, that they had a reasonable expectation of continued service. *See* Order 888-A, ¶ 31,048 at 30,394-95. This finding rested on two considerations: that the burden of unrecoverable stranded costs could impair utilities' access to capital markets, which could in turn precipitate the departure of other customers, thus worsening the utilities' financial condition and threatening its ability to provide reliable service; and that allowing customers to leave a utility without paying their share of costs would shift those costs to other customers who lack alternative power sources. *See* Order 888, ¶ 31,036 at 31,811. For its second generic finding, FERC concluded that it was in the public interest

to allow customers to modify their wholesale requirements contracts in any way upon a showing that the terms are no longer just and reasonable. *See* Order 888-A, ¶ 31,048 at 30,189. Observing that the contracts in question "were entered into during an era in which transmission providers exercised monopoly control over access to their transmission facilities," FERC based this finding on the unequal bargaining power between utilities and customers. *Id.* at 30,193. Because "[m]any of these contracts were the result of uneven bargaining power between customers and monopolist transmission providers," FERC reasoned, "the unprecedented competitive changes that have occurred (and are continuing to occur) in the industry may render their contracts to be no longer in the public interest or just and reasonable." *Id.*

Challenging the first finding, POSCR argues that FERC lacks authority to make a *generic* public interest finding that (59)allows for contract modification in an entire class of cases. POSCR insists that FERC can only proceed on a case-by-case basis, determining in each case whether a particular contract modification is in the public interest. Even if FERC has authority to make generic findings, POSCR goes on to argue, FERC's Order 888 finding is unsupported by substantial evidence. The investor owned utilities ("IOUs") challenge the second finding, arguing that allowing customers to seek modification of all contract terms, while limiting utilities to stranded cost provisions, fails adequately to balance competing interests.

a. *FERC's authority to make a generic public interest finding*

POSCR correctly observes that FERC has pointed to no case in which a court affirmed a generic *Mobile-Sierra* finding. At the same time, POSCR has cited no case prohibiting FERC from making a generic finding, nor have we found one. In the absence of definitive authority in either direction, and given the unique circumstances of this case and our traditional deference to

FERC's expertise, we find no fault with FERC's generic determination.

The *Mobile-Sierra* doctrine "represents the Supreme Court's attempt to strike a balance between private contractual rights and the regulatory power to modify contracts when necessary to protect the public interest." *Northeast Utilities Serv. Co. v. FERC*, 55 F.3d 686, 689 (1st Cir. 1995). In *Mobile*, the Supreme Court recognized that intervening circumstances may create a situation in which contractual terms and conditions that were just and reasonable at the time the contract was executed are no longer just and reasonable. 350 U.S. at 344-45. But concluding that a utility is not typically "entitled to be relieved of its improvident bargain," the *Sierra* Court required that FERC's predecessor, the Federal Power Commission, show more than that the contract was unjust and unreasonable—the Commission had to find that contract modification was in the public interest. 350 U.S. at 355.

In most cases, intervening circumstances are unique to the relationship between contracting parties. *See, e.g. Northeast* (60)*Utilities*, 55 F.3d 686 (affirming FERC's modification to the rate schedule of a contract as a condition for approval of a merger between two parties to the contract). But where intervening circumstances—in this instance, FERC-mandated open access transmission—affect an entire class of contracts in an identical manner, we find nothing in the *Mobile-Sierra* doctrine to prohibit FERC from responding with a public interest finding applicable to all contracts of that class. Moreover, in providing for stranded cost recovery, FERC has not relieved utilities of "improvident bargains," the concern of the *Sierra* Court; rather, it has recognized that open access affects all utilities in the same manner, namely leaving them vulnerable to potentially unrecoverable stranded costs. In fact, to deny FERC authority to make generic findings in such a case would simply

impose on it and the parties the repetitive burden of proving the public interest in each and every case.

In sustaining FERC's generic finding, we are influenced by the fact that before recovering stranded costs, a utility must prove that it had a reasonable expectation of continued service to a particular customer. As the IOUs intervening on behalf of FERC explain, the need to make this showing adds a particularized element to FERC's generic public interest finding. Viewed this way, Order 888's generic finding is more precisely stated as follows: It is in the public interest to allow utilities to recover stranded costs if they can prove that they had a reasonable expectation of continued service to particular customers. If a utility can demonstrate that it had a reasonable expectation of continued service to a particular customer, and incurred costs based on that expectation, then it would be against the public interest to require other customers or shareholders to bear those costs. As Order 888 explains, "the case-by-case findings that some commenters seek will, in effect, be made when the Commission determines whether to approve a proposed stranded cost amendment to a particular contract." Order 888, ¶ 31,036 at 31,813.

We stress that generic *Mobile-Sierra* findings are appropriate only in rare circumstances. Order 888 is just such a circumstance. It fundamentally changes the regulatory envi-(61)ronment in which utilities operate, introducing meaningful competition into an industry that since its inception has been highly regulated and affecting all utilities in a similar way.

b. *FERC's stranded cost public interest finding*

Having concluded that the *Mobile-Sierra* doctrine permits a generic finding in this case, we turn to POSCR's claim that the finding was unsupported by substantial evidence. POSCR faults FERC for failing to adduce evidence to support its conclusion

that denying stranded cost recovery would put particular utilities in financial peril. POSCR also thinks that the impact on customers of failing to provide for stranded cost recovery is insufficient to support a public interest finding.

With respect to POSCR's first point, it is certainly true that *Sierra* identified impairment of "the financial ability of the public utility to continue its service" as one factor supporting a public interest finding. *Sierra*, 350 U.S. at 355. Relying on this, POSCR challenges FERC's public interest finding on the ground that the record contains no individual assessments of the financial condition of public utilities.

Although public interest findings made on a case-by-case basis necessarily evaluate the harm to the particular utility seeking modification, that is not true where, as here, FERC implements a generic change in the industry. Just as that change can support a generic public interest finding, that generic finding can be supported by generic industry-wide evidence. FERC has produced such evidence. The record contains estimates of stranded costs amounting to $200 billion or more. *See* Stranded Cost NOPR, ¶ 32,507 at 32,866. It also includes comments from representatives of the financial community stating that "the prospect of not recovering stranded costs could erode a utility's ability to attract capital."

POSCR points out that eighty-five to ninety percent of the estimated $200 billion of stranded costs relates to retail sales, not wholesale sales. True enough, but we find no basis for questioning FERC's conclusion that unrecovered stranded (62)costs of even ten percent of $200 billion—the low end of the wholesale stranded cost estimate—could have serious consequences for utilities. *See* Order 888, ¶ 31,036 at 31,790. In any event, if POSCR turns out to be correct about the absence of a wholesale stranded cost problem, few utilities will avail themselves of Order 888's stranded cost recovery provisions.

POSCR's second argument focuses on FERC's finding that "if some customers are permitted to leave their suppliers without paying for stranded costs, this may cause an excessive burden on the remaining customers who, for whatever reason, cannot leave and therefore may have to bear those costs." Order 888, ¶ 31,036 at 31,811. POSCR does not agree with FERC that the failure to recover stranded costs will create an "undue burden" on remaining customers. But disagreeing with FERC is not enough. To prevail in this court, POSCR must demonstrate that FERC's prediction that failure to recover stranded costs will create an undue burden on remaining customers is unsupported by substantial evidence, *see* 16 U.S.C. § 825*l*(b), which is another way of saying it is arbitrary and capricious. *See Michigan Consolidated Gas Co. v. FERC*, 883 F.2d 117, 124 (D.C. Cir. 1989) ("[M]aking ... predictions is clearly within the Commission's expertise and will be upheld if rationally based on record evidence.") (internal quotation marks omitted). This POSCR has failed to do.

c. *FERC's public interest finding regarding customers*

The IOUs mount two challenges to FERC's second public interest finding—that it was in the public interest to allow customers to seek modification of their wholesale requirements contracts. Unlike POSCR, the IOUs make no claim that the finding lacks substantial evidence; rather, they contend that FERC's decision to allow customers to seek modification of *all* contract terms, while limiting utilities to adding stranded cost provisions, fails to balance FERC's competing concerns: respecting existing contractual commitments and accelerating the transition to competition. They also complain that FERC has failed adequately to explain (63)why affording customers this broad ability to modify their contracts is in the public interest.

FERC gave two justifications for affording customers a broader opportunity than utilities to modify their contracts, both

of which seem perfectly rational to us. First, Order 888-A explains, "these contracts were entered into during an era in which transmission providers exercised monopoly control over access to their transmission facilities." Order 888-A, ¶ 31,048 at 30,193. Also, the "unprecedented competitive changes .... may affect whether such contracts continue to be just and reasonable or not unduly discriminatory both as to the direct customers of the contracts, as well as to indirect, third-party consumers...." *Id.* at 30,193-94. In fact, Order 888 rests on the very premise that by denying competitors access to their transmission lines, utilities engaged in undue discrimination. Confined to purchasing power from their local utilities, customers suffered from this lack of access. In the natural gas restructuring, we affirmed FERC's decision to allow customers to seek to modify their sales contracts because those contracts "necessarily reflect the pipelines' monopoly power." *AGD*, 824 F.2d at 1017. The same reasons call for affirming FERC's decision here. In addition, as FERC has explained, the harm to third parties (*i.e.*, customers of the wholesale requirements customers) that may result from adherence to uneconomical contracts further justifies its conclusion. *See* Order 888-A, ¶ 31,048 at 30,194. Remedying potential unfairness to utilities by allowing them to seek stranded cost recovery if a customer shortens the term of a contract, FERC struck a balance between customers and utilities that can hardly be characterized as arbitrary or capricious.

4. *Availability of Stranded Cost Recovery to Nonjurisdictional Utilities and G&T Cooperatives*

Section 201 of the FPA gives FERC jurisdiction over "public utilities" but not over federal and state utilities. 16 U.S.C. § 824. Although FERC required utilities not subject to its jurisdiction ("nonjurisdictional utilities") to provide reciprocal open access transmission when they use a jurisdic-(64)tional utility's open access tariff, it declined to provide a mechanism for them to recover stranded costs. Explaining that it promulgated its

reciprocity provision pursuant to fairness concerns, not statutory authority, FERC reasoned that it lacked jurisdiction to provide stranded cost recovery for nonjurisdictional utilities. *See* Order 888-A, ¶ 31,048 at 30,364. FERC recommended that these utilities include stranded cost provisions in their open access tariffs; those tariffs would be reviewed not by FERC but by the appropriate regulatory authority. *See id.*

Dairyland petitioners contend that FERC acted arbitrarily and capriciously in denying nonjurisdictional utilities stranded cost recovery, arguing that the same "fairness" concerns invoked by FERC to require reciprocal open access transmission require the award of stranded costs. To be sure, FERC may have had authority to include stranded cost recovery as a provision of Dairyland's open access tariff. But Dairyland has offered no reason for thinking that FERC's refusal to do so was arbitrary and capricious. Given the limited scope of FERC's stranded cost provisions, its lack of jurisdiction over entities like Dairyland, and the ability of nonjurisdictional utilities to include stranded cost provisions in their open access tariffs, we see no reason to question FERC's judgment on this issue.

The same is true with respect to the transmission-dependent utilities ("TDUs"). Like the Dairyland petitioners, they claim that FERC acted arbitrarily and capriciously by failing to provide a mechanism for them to recover stranded costs. Owning few or no transmission facilities, TDUs serve their loads using other utilities' transmission systems. Not only are TDUs nonjurisdictional utilities, but, as Order 888-A explains, open access does not cause their costs to become stranded—their customers have always had an option to use other utilities' transmission services to purchase power. *See* Order 888-A, ¶ 31,048 at 30,365.

Dairyland also contends that FERC acted arbitrarily and capriciously when it declined to treat a generation and

transmission ("G&T") cooperative and its member distribution (65)cooperatives as a single economic unit for stranded cost purposes. G&T cooperatives provide bundled wholesale power to their member distribution cooperatives, who in turn sell the power to the members' retail customers. Observing that cooperatives, unlike traditional utilities, are not vertically integrated but instead function as single economic units, Dairyland claims that G&T cooperatives have reasonable expectations of continued service to retail customers of their member cooperatives that differ substantially from the expectations public utilities have with respect to retail customers of their wholesale customers. This difference, Dairyland argues, requires FERC to allow G&T cooperatives to recover stranded costs from their member cooperatives' customers.

Rejecting Dairyland's petition for rehearing on this point, FERC noted that treating a G&T cooperative and its members as a single economic unit for purposes of stranded cost recovery would conflict with its treatment of these same cooperatives as distinct entities in its reciprocity provisions. Order 888-A, ¶ 31,048 at 30,366. There, FERC agreed with Dairyland's proposal that if a G&T cooperative seeks open access transmission from a public utility, "then only the G&T cooperative, and not its member distribution cooperatives, would be required to offer [reciprocal] transmission service." Order 888, ¶31,036 at 31,763. Moreover, FERC reasoned, recovering from a retail customer of a member cooperative is, in effect, recovering from an indirect customer, a situation that FERC declined to include in its stranded cost rule. *See* Order 888-A, ¶ 31,048 at 30,366.

It is true that FERC could have treated G&T cooperatives and their members as single economic units for stranded cost purposes. But FERC's explanation of why it chose not to do so, particularly the fact that G&T cooperatives and their members

were treated as distinct entities for reciprocity purposes, is entirely reasonable.

5. *Challenges to Technical Aspects of Order 888's Stranded Cost Recovery Provisions*

Several petitioners mount challenges to various technical aspects of the stranded cost recovery provisions. Before (66)addressing these challenges, we emphasize the very limited scope of our review. For us to undo what FERC has done, petitioners must persuade us that FERC's actions were arbitrary or capricious. "Highly deferential," the arbitrary and capricious standard "presumes the validity of agency action." *National Mining Ass'n v. Mine Safety and Health Admin.*, 116 F.3d 520, 536 (1997). Where, as here, the issue before us "requires a high level of technical expertise, we must defer to the informed discretion of the responsible federal agencies." *Marsh v. Oregon Natural Resources Council*, 490 U.S. 360, 377 (1989) (internal quotation marks omitted). It is not enough for petitioners to convince us of the reasonableness of their views, *see UDC*, 88 F.3d at 1169 ("The existence of a second reasonable course of action does not invalidate an agency's determination."); those arguments should be presented to FERC, whose commissioners are appointed by the President and confirmed by the Senate with the expectation that they, not Article III courts, will make policy judgments.

To prevail in this court, petitioners must demonstrate that *FERC's* policy judgments are arbitrary or capricious, a heavy burden indeed. *See National Treasury Employees Union v. Hefler*, 53 F.3d 1289, 1292 (D.C. Cir. 1995) ("The 'scope of review under the "arbitrary and capricious" standard is narrow and a court is not to substitute its judgment for that of the agency.'") (quoting *Motor Vehicles Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983)). With this very

deferential scope of review in mind, we turn to petitioners' arguments.

a. *POSCR's challenges to the stranded cost formula*

Reasoning that it would be burdensome to identify each and every asset that would become underutilized as a result of Order 888, FERC adopted a "revenues lost" formula to determine a departing customer's stranded cost obligation. Order 888, ¶ 31,036 at 31,839. For each year a utility can prove that it had a reasonable expectation of continued service to a particular customer, the formula calculates the customer's stranded cost obligation by subtracting the com-(67)petitive market value of the power the customer would have purchased from the utility (as estimated by the utility) from the amount the customer would have paid had it remained a generation customer of the utility (based on FERC-approved rates that the customer paid the prior three years). *Id.* At 31,839-40.

POSCR claims that this formula gives utilities no incentive to mitigate their stranded costs. Not so. The formula automatically provides such an incentive by subtracting from utilities' recovery the market price of the power—utilities that fail to sell the power at market prices will not recover their full costs. POSCR also claims that the formula fails accurately to measure stranded costs because it is based on an estimate of those costs at one point in time. Responding, FERC explained why it rejected a "true-up" provision that would have made adjustments to the amount the customer owed to reflect market conditions over the reasonable expectation period. According to FERC, such an approach would have created enormous uncertainty, outweighing any potential increase in accuracy. *See* Order 888-A, ¶ 31,048 at 30,427-28. POSCR has offered no basis for us to question this reasoning.

POSCR's claim that the formula gives utilities an incentive to minimize their estimate of the market value of the power the customer would have purchased is similarly groundless. To avoid precisely this result, Order 888 gives customers an option to either market or broker the capacity and associated energy they would have purchased from their historic utility, effectively reducing their stranded cost obligations by the difference between the actual market value of the power and the utility's estimate of the market value. *See* Order 888, ¶ 31,036 at 31,844. Order 888 also gives customers an option to substitute the price of power under the customer's contract with a new supplier for the utility's estimate of the market value. *See id.*

One final point. Throughout its brief and at oral argument, POSCR consistently referred to stranded costs as "imprudently incurred costs." Although it never developed this (68)argument, we think it worth noting that all costs included in customers' stranded cost obligations are based on FERC-approved rates and were included in utility rate bases as assignable to particular customers. To us, this means that these costs are legitimate, prudent, and verifiable.

b. *Inclusion of known and measurable costs*

The IOUs take issue with Order 888's stranded cost recovery formula because the estimate of the price the customer would have paid for the power is based on rates for the prior three years; according to the IOUs, this approach fails to consider known and measurable costs resulting from regulatory mandates that may have been deferred pursuant to filed rate schedules and FERC-approved settlements. The costs they cite include deferred costs of generation that have already been approved for inclusion in the rate base, costs relating to approved qualifying facility contracts, and government-imposed costs such as deferred taxes and nuclear decommissioning.

Although it is true that the revenue calculation measures only current rates and not deferred costs, Order 888 allows customers and utilities to file for a change in the rates before the customer's requirements contract terminates; in such cases, FERC will calculate the customer's stranded cost obligation based on those new rates. *See* Order 888-A, ¶ 31,048 at 30,427. While seeking to avoid detailed listings of specific costs that may become stranded, FERC has adequately preserved utilities' ability to include known, measurable costs in revenue estimates through a ratemaking proceeding.

c. *Treatment of energy costs in the market option*

The IOUs challenge FERC's treatment of energy costs in the market option. To mitigate utilities' incentives to minimize their estimates of the market value of the power (the competitive market value estimate or "CMVE"), Order 888 affords customers an option to buy the power stranded by their departure from the utility and resell it. Order 888, ¶ 31,036 at 31,844. Customers would purchase generation (69)capacity at the utility's estimated market value of the capacity and associated energy at average system variable cost. *Id.* At 31,845. Thus if a customer believes that a utility is underestimating the price at which it could sell the power, the customer can buy the power and then resell it. While customers exercising this option would still have to pay their stranded cost obligation as calculated under the formula, they would effectively offset the obligation by keeping the profit on the resale of the power. *Id.* At 31,845 n.879.

The IOUs contend that allowing customers to pay *average variable cost* for the associated energy is inconsistent with Order 888's definition of the CMVE, which equals the *market value* of both the generation capacity and associated energy. *See id.* At 31,839 (defining CMVE as "the utility's estimate of the average annual revenues ... that it can receive by selling the released

capacity and associated energy, based on a market analysis performed by the utility"). Customers could receive a windfall, the IOUs claim, by exercising the market option although they will pay average variable cost for the associated energy, they will be able to resell it at the presumably higher market price. At the same time, utilities will be unable to recover the full market value of the power because they will be forced to sell the associated energy at cost.

Responding to this argument in Order 888-A, FERC offered two justifications for allowing customers to purchase the associated energy at average variable cost. First, because the capacity being marketed would not generally be associated with a single asset, customers exercising this option are purchasing a "slice of the system" and thus should pay average variable cost. Second, customers should be able to purchase energy at the price they currently pay, typically average variable cost. *See* Order 888-A, ¶ 31,048 at 30,433. But neither explanation responds to the IOUs' argument that defining CMVE as the market price of both the capacity and associated energy is *inconsistent with* allowing customers exercising the market option to purchase associated energy at average variable cost. In its brief in this court, FERC continues to misapprehend the IOUs' argument, largely reit-(70)erating the same arguments and failing to address the inconsistency.

The market option's stated intention is to reduce a utility's incentive to understate the CMVE. *See* Order 888, ¶ 31,036 at 31,842. If it did understate the CMVE, then customers could buy the power from the utility and resell it, keeping the difference. But FERC's policy of allowing customers to purchase the associated energy at cost gives customers an incentive to exercise the market option even when a utility has appropriately estimated CMVE because they can buy the energy at cost and resell it at the presumably higher market price. FERC's failure to explain whether it intended this result and if so, the justification

for permitting customers to receive a windfall while undercompensating utilities constitutes a failure of reasoned decisionmaking. *See AGD*, 824 F.2d at 1030 ("We do not require that FERC reach any particular conclusion; we merely mandate that it reach its conclusion by reasoned decisionmaking."). We therefore vacate this portion of the orders and remand the issue to FERC for further consideration.

d. *Rescission of notice of termination provision*

Until FERC issued Orders 888 and 889, it had required parties to power sales contracts to notify it sixty days prior to cancellation of a contract or termination of a contract by its own terms. *See* 18 C.F.R. § 35.15 (repealed by Order 888). Orders 888 and 889 eliminate the requirement that parties notify FERC in advance when a contract terminates *by its own terms*, but only with respect to contracts executed after July 9, 1996; in other cases of contract cancellation or termination, parties must still notify FERC in advance. *See* 18 C.F.R. § 35.15 (1999). TDU petitioners claim that in rescinding the notice requirement, FERC ignored the fact that utilities still have substantial market power. That some utilities retain market power in generation, however, does not undermine Orders 888 and 889. Through these orders, FERC sought to move the electricity industry toward competition; by providing an open access mechanism through which buyers may purchase power from suppliers other than trans-(71)mitting utilities, FERC substantially reduced utilities' market power. Eliminating the notice requirement furthered that policy. Moreover, customers who believe termination of their contracts is unjust can seek relief from FERC pursuant to section 206 of the FPA. *See* Order 888-A, ¶ 31,048 at 30,393.

e. *Provision for benefits lost*

The TDU petitioners claim that FERC acted arbitrarily and capriciously by failing to provide a mechanism for customers

purchasing power at below-market rates to preserve those rates at the termination of their contract with their historic utility. Just as utilities may have expectations of continued service to particular customers, the TDU petitioners contend, customers may have reasonable expectations of continuing to receive wholesale requirements service from their historic utility at cost-based rates. Order 888-A says that the Commission does "not have a sufficient basis on which to make generic findings that customers under such contracts may be entitled to extend a contract at the existing rate." Order 888-A, ¶ 31,048 at 30,393 (emphasis removed). Moreover, the order explains, "the consequences of customers' expectations as a general matter would not have the potential to shift significant costs to other customers," whereas utilities' failure to recover stranded costs could potentially shift the costs to other customers. *Id.*

We think that FERC has adequately explained why it chose not to provide for benefits-lost recovery in Order 888. Most important, FERC has not foreclosed customers in this situation from seeking relief: As Order 888-A explains, a customer may "exercise its procedural rights under section 206 to show that the contract should be extended at the existing contract rate, or [ ] make such a showing in the context of a utility's proposed termination of a contract pursuant to the section 35.15 notice of termination (approval) requirement." *Id.* (footnote omitted). Given that agencies "enjoy[ ] broad discretion in determining how best to handle related, yet discrete, issues in terms of procedures ... and priorities," we think FERC's refusal to promulgate a generic rule on this issue was entirely reasonable. *Mobil Oil Explo(72)ration & Producing Southeast, Inc. v. United Distrib. Cos.*, 498 U.S. 211, 230 (1990).

B. *Retail Stranded Costs*

Recognizing state agency authority to address stranded costs that relate to retail power sales, Order 888 limits FERC's role as

a forum for the recovery of these costs to two situations: when customers take advantage of state-ordered wheeling to reach new power suppliers and when former retail customers become wholesale customers through what is known as municipalization or municipal annexation. *See* Order 888-A, ¶ 31,048 at 30,402, 30410. In the former scenario, FERC will consider proposals for the recovery of stranded costs only when the appropriate state regulatory commission lacks authority to do so; in the latter situation, FERC will serve as the primary forum for resolution of stranded cost claims.

1. *Stranded Costs Arising from Retail Wheeling*

Stranded costs may result from state unbundling of retail sales, where retail customers take advantage of state-ordered retail wheeling to reach new generation suppliers. *See* Order 888, ¶ 31,036 at 31,819. Observing that both FERC and the states have authority to address these stranded costs, Order 888 explains that:

> [B]ecause it is a state decision to permit or require the retail wheeling that causes retail stranded costs to occur, we will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required.

Order 888, ¶ 31,036 at 31,824-25 (footnote omitted). FERC will provide for recovery of those stranded costs through the transmission rate the former supplying utility charges the departing customer. Order 888-A, ¶ 31,048 at 30,410. (As discussed in Section III *supra*, FERC has jurisdiction over

(73)the transmission component of unbundled retail sales.) In evaluating claims for stranded cost recovery, FERC will use the same standards as it applies with respect to wholesale stranded costs (*i.e.*, it will require utilities to demonstrate a reasonable expectation of continued service). *See* Order 888, ¶ 31,036 at 31,819 n.722.

Two sets of petitioners challenge FERC's retail stranded cost recovery provisions from opposite sides. The States and POSCR contend that FERC exceeded its jurisdiction by asserting rate authority over retail stranded costs. The IOUs argue that FERC abdicated its statutory authority by failing to agree to consider *all* proposals for recovery of stranded costs that arise from retail wheeling. Because we think FERC has appropriately exercised its jurisdiction, we reject both claims.

a. *FERC's jurisdiction over retail stranded costs*

The States' and POSCR's arguments boil down to the following: Because retail stranded costs relate primarily to facilities used for retail generation, and because section 201(b) of the FPA explicitly excludes these facilities from FERC's jurisdiction, FERC may not provide for recovery of these costs in FERC-jurisdictional rates. Unbundling electricity sales, they argue, cannot alter the jurisdictional status of these costs.

As an initial matter, we agree with FERC that petitioners confuse costs and rates. Rates are jurisdictional; costs are not. As Order 888-A explains:

> [T]here are rarely separate retail and wholesale generating facilities. Retail customers and wholesale requirements customers get energy from the same facilities, each buying a "slice of the system." Typically all generating assets go into both the retail and the wholesale rate bases for

> determining retail and wholesale rates. Rates are determined by allocating the total generating costs among customer classes. The parties confuse the issue before us to the extent they suggest that state commissions, not this Commission, have "jurisdiction" over cer-(74)tain "costs." Neither the state commissions nor this Commission has exclusive jurisdiction over "costs." Each regulatory authority has jurisdiction to determine "rates" for services subject to its jurisdiction and, in determining rates, may take into account all of the costs incurred by the utility.

Order 888-A, ¶ 31,048 at 30,414. In other words, as FERC explained in its brief, "regulatory authorities do not carve out so-called 'wholesale costs' that only FERC can take into account in determining rates subject to its jurisdiction or so-called 'retail costs' that only a state commission can take into account in determining rates subject to state jurisdiction." Instead, "[u]nder historical cost-of-service ratemaking, each regulatory authority, in exercising its respective *ratemaking* jurisdiction, reviews the *total* costs incurred by a utility to provide service and makes its separate and independent determination of what costs may be recovered through rates within its jurisdiction." Order 888-A, ¶ 31,048 at 30,414.

Thus, while petitioners correctly point out that section 201(b) of the FPA denies FERC jurisdiction over "facilities used for the generation of electric energy," that provision does not necessarily prevent FERC from including *costs* relating to generating facilities in transmission *rates*, over which FERC indisputably has jurisdiction. 16 U.S.C. § 824(b). This is so because this part of section 201(b) is modified by the phrase "except as specifically provided in this subchapter and subchapter III of this chapter." *Id.* Given that section 201(a) grants FERC jurisdiction over "the transmission of electric energy in interstate commerce" and,

therefore, over transmission rates, 16 U.S.C. § 824(a), FERC may exercise jurisdiction over generation facilities to the extent necessary to regulate interstate transmission.

This is exactly the construction that we gave section 201(b) in *Mississippi Industries v. FERC*, 808 F.2d 1525, 1543-45 (D.C. Cir. 1987) (subsequent history omitted). There, petitioners challenged FERC's authority to reallocate costs relating to generation facilities among utilities that were parties to a power sales agreement. Justifying its authority to reallo-(75)cate such costs, FERC relied on its "undisputed jurisdiction over interstate sales of electric energy at wholesale." *Id.* At 1543. We agreed: "[A]lthough allocating cost does, to some extent, result in the 'regulation of matters relating to generation,' such regulation is valid under the FPA when it is the byproduct of a legitimate exercise of FERC's power to regulate wholesale rates." *Id.* In reaching this conclusion, we rejected petitioners' argument that "the statutory prohibition of federal regulation of [generation] facilities in section 201(b) becomes meaningless if FERC is permitted to allocate the costs of a plant," given FERC's undisputed responsibility to regulate the wholesale sale of power. *Id.* At 1543-44. Under *Mississippi Industries*, then, FERC may regulate costs relating to generation facilities if such regulation "is the byproduct of a legitimate exercise of FERC's power to" regulate interstate transmission. *Id.* At 1543. Because FERC indisputably has jurisdiction over transmission rates, *Mississippi Industries* also disposes of petitioners' argument that FERC's retail stranded cost recovery provisions run afoul of section 201(a) of the FPA, which provides that "Federal regulation [shall] extend only to those matters which are not subject to regulation by the States." 16 U.S.C. § 824(a).

Attempting to distinguish *Mississippi Industries*, petitioners point out that the case "involved authority to allocate generation costs to a wholesale *sales* rate (which may, of course, include generation costs)." True, but *Mississippi Industries* provides

clear authority for the proposition that there is no per se *jurisdictional* bar to FERC's including generation costs in jurisdictional rates, whether wholesale sales rates or transmission rates. Thus narrowed, the question before us is this: Is inclusion of stranded costs relating to generation facilities in transmission rates the byproduct of a legitimate exercise of FERC's authority over transmission rates? In most cases the answer would be no, but given the highly unusual circumstances of this case, we think the answer is yes. Just as FERC may include generation-related *wholesale* stranded costs in transmission rates (*see* Section V.A.1.b), it may include generation-related *retail* stranded costs in transmission rates. That retail stranded costs were (76)originally reflected in state-jurisdictional retail sales rates does not change the analysis, for in both cases the stranded costs can be viewed as "costs" of providing transmission services: "While such costs are not a cost of operating the physical transmission system, nevertheless, they are an economic cost incurred as a result of being required to provide retail transmission." Order 888-A, ¶ 31,048 at 30,414 n.708. While we agree that generation-related retail costs are not typically "costs" relating to transmission services, the fundamental changes wrought by state-ordered retail wheeling, as well as the narrow circumstances in which FERC will consider stranded cost recovery claims, justify the conclusion that these costs are costs of providing transmission service.

Petitioners claim that by agreeing to consider retail stranded cost recovery claims, FERC has unduly interfered with state legislative processes and decisions. We disagree. FERC has limited its "interference" to instances where state commissions have no authority even to *address* stranded cost recovery claims. Describing its role as limited to "fill[ing] any regulatory gap," FERC made it clear that it will deny consideration to any utility seeking stranded cost recovery "if a state regulatory authority with authority to address retail wheeling stranded costs has in fact addressed such costs, regardless of whether the state

regulatory authority has allowed full recovery, partial recovery, or no recovery." Order 888-A, ¶ 31,048 at 30,415. Under these circumstances, it can hardly be said that FERC has usurped state authority.

b. *FERC's refusal to assert jurisdiction over all retail stranded costs*

Contending that FERC did not go far enough, the IOUs challenge the agency's refusal to consider claims for stranded costs resulting from state-ordered retail wheeling unless the relevant state regulatory commission lacks authority to address such claims. They claim that FERC should have agreed to consider proposals for retail stranded cost recovery whether or not the state commission had authority to address the claim, and even whether or not a state commission with such authority had already addressed the claim. In support (77)of their position, the IOUs advance three related arguments. They allege first that by concluding that it had jurisdiction over retail stranded costs but declining to exercise it, FERC abdicated its legal authority. Second, they say, FERC violated its statutory obligation to ensure just and reasonable rates. And finally, they contend that FERC erred in concluding that stranded costs resulting from retail wheeling lack a direct nexus to the open access transmission ordered in Order 888.

With respect to their first argument, the IOUs claim that once FERC determined that it had jurisdiction over retail stranded costs, the agency had to exercise that jurisdiction. In making this argument, the IOUs make the same mistake POSCR made: They confuse FERC jurisdiction over *costs* with its jurisdiction over *rates*. FERC has not "concluded that it shares jurisdiction over retail stranded costs with the states," as the IOUs assert. As we explained above, "costs" are not jurisdictional. The FPA speaks not in terms of "costs," but in terms of "rates," requiring FERC to ensure that rates are just, reasonable, and not unduly

discriminatory. FERC indisputably has jurisdiction over interstate transmission rates. In essence, then, the IOUs claim that FERC has no discretion to leave retail stranded cost recovery to state authorities.

We review claims that an agency lacks discretion to follow (or decline to follow) a certain course of action by examining the agency's governing statute as well as its own regulations. *See, e.g., National Wildlife Federation v. Browner*, 127 F.3d 1126, 1130 (D.C. Cir. 1997) (concluding that agency regulations do not require EPA to review and approve or disapprove a state's decision to maintain existing water quality standards); *NRDC v. EPA*, 25 F.3d 1063, 1069-70 (D.C. Cir. 1994) (holding that neither the governing statute nor relevant regulations impose a mandatory duty on EPA to list all wastes that exhibit a hazardous characteristic; statute gives EPA "substantial room to exercise its expertise in determining the appropriate grounds for listing"). The IOUs have failed to point to any statutory provision that robs FERC of discretion to decide, as a matter of policy, that state regulato-(78)ry commissions should serve as the primary forum for retail stranded cost recovery. Our own examination of the FPA reveals no such provision either. Sections of the statute giving FERC jurisdiction over transmission in interstate commerce, 16 U.S.C. § 824(a), and requiring FERC to ensure that rates are just and reasonable, 16 U.S.C. § 824d(a), do not alone create a mandatory duty to consider proposals for retail stranded cost recovery.

The two Supreme Court cases the IOUs rely on provide no support for their position, for in both cases the agencies, unlike FERC in this case, failed to comply with a specific statutory mandate. In *MCI v. AT&T*, 512 U.S. 218 (1994), the Supreme Court held that the FCC could not exempt certain communication common carriers from filing a tariff; the statute specified that *all* carriers must file tariffs. Similarly, in *FPC v. Texaco, Inc.*, 417 U.S. 380 (1974), the Supreme Court

determined that the FPC could not exempt certain producers from the statute's requirement that rates be just and reasonable. Under these cases, FERC would abdicate its statutory obligations if it, for example, exempted certain utilities from the requirement that rates be just and reasonable (as in *Texaco*), or if it refused to review transmission rate filings altogether. These cases do not hold that in carrying out its statutory obligations, FERC has no discretion to determine as a matter of policy that states are better positioned to address costs originally included in retail rate bases. What the IOUs suggest—that because FERC has *authority* to address retail stranded costs through transmission rates, it must exercise that authority—is simply not the law.

As an alternative to their legal argument, the IOUs claim that FERC acted arbitrarily and capriciously in determining that just and reasonable transmission rates include retail stranded cost recovery in some circumstances but not in others. Their argument goes like this: Section 201(b)(1) of the FPA gives FERC exclusive jurisdiction over transmission of electric energy in interstate commerce. Under section 205, FERC must set just and reasonable rates. In addition, sections 205 and 206 prohibit undue discrimination. Thus, (79)the IOUs argue, "[b]y approving different transmission rates, some including stranded cost recovery (*e.g.*, municipalization), and others without (*e.g.*, retail wheeling or bypass), FERC is sanctioning arbitrary and capricious differences in violation of the FPA."

In making this argument, the IOUs ignore the wide discretion the FPA affords FERC to determine what constitute "just and reasonable rates" and "undue discrimination," as well as the unusual circumstances created by an industry change as fundamental as order 888's open access requirement. Just because some transmission rates include retail stranded costs while others do not does not alone make Order 888 arbitrary and capricious; rather, petitioners must show that there is no reason

for the difference. *Cf. AGD*, 824 F.2d at 1009 ("[T]he mere fact of a rate disparity is not enough to constitute unlawful discrimination.") (internal quotation marks omitted). We think FERC has provided a convincing explanation for the difference. "Recovery of this type of cost through a transmission rate is obviously not the norm," explains Order 888-A, "but is necessitated by the need to deal with the transition costs associated with this Rule." Order 888-A, ¶ 31,048 at 30,418. Only in situations where state regulatory commissions lack authority to award stranded costs will FERC include these costs in transmission rates. Otherwise, customers would be able to avoid their stranded cost obligations, leaving utility shareholders or remaining customers to bear the costs.

The IOUs reliance on the natural gas restructuring cases is misplaced. Setting aside the extraordinary nature of take-or-pay liabilities as compared to the stranded costs at issue here, *AGD* required only that FERC *address* the take-or-pay liabilities that the pipelines had incurred. *See AGD*, 824 F.2d at 1030 ("We do not require that FERC reach any particular conclusion; we merely mandate that it reach its conclusion by reasoned decisionmaking."). That is exactly what Order 888 does with respect to stranded costs. While FERC has not agreed to serve as the forum for recovery of these costs in all situations, neither the FPA nor the natural gas cases requires it to do so. By ensuring that utilities have a forum in which (80)to bring claims for retail stranded cost recovery, FERC has done just what *AGD* requires.

Nor do we find merit in the IOUs' argument that FERC erred in concluding that stranded costs resulting from retail wheeling lack a direct nexus to the open access transmission mandated by Order 888. FERC's decision that state regulatory commissions should address retail stranded costs rested on its conclusion that state-ordered wheeling, not FERC-mandated open access transmission, causes those costs to become stranded. *See* Order

888-A, ¶ 31,048 at 30,410. Recognizing a "limited" nexus between retail stranded costs and FERC-mandated open access stemming from FERC's jurisdiction over transmission rates and the resulting authority to award stranded costs, FERC nonetheless found *no causal nexus* between stranded costs and FERC-ordered transmission. *Id.* At 30,419. The lack of a direct causal nexus differentiates retail stranded costs from retail-turned-wholesale stranded costs (*see infra* Section V.B.2).

Taking issue with this reasoning, the IOUs contend that FERC ignored "the central role played by the federal government" in shaping the electric energy industry. Because retail wheeling, according to the IOUs, is "a direct result of a federally created system of increased competition," FERC must take responsibility for all retail stranded costs.

Nowhere does FERC contest the nexus between state-ordered wheeling and order 888's open access requirement. But the existence of a nexus does not require FERC to address retail stranded costs in light of the fact that in most instances state regulatory commissions will have authority to do so. Indeed, because the costs were originally included in retail rate bases, state agencies are better positioned to consider them. Given that it is state-ordered wheeling that most directly causes retail costs to become stranded, we find no reason to disturb FERC's judgment.

2. *Stranded Costs Relating to Retail-Turned-Wholesale Customers*

FERC concluded that open access transmission may encourage what is known as "municipalization," where a town (81) condemns a utility's distribution plant, becomes a wholesale customer of the utility, and utilizes open access transmission to purchase power on the competitive market. Concluding that costs incurred to serve former retail customers may become

stranded due to the municipality's (the new wholesaler's) utilization of open access transmission, FERC decided to serve as the primary forum for resolution of stranded costs claims relating to new municipalizations. *See* Order 888-A, ¶ 31,048 at 30,402. FERC also decided to serve as the primary forum "in a discrete set of municipal annexation cases"—*i.e.*, cases involving "existing municipal utilities that annex retail customer service territories and, through the availability of Commission-required transmission access, use the transmission system of the annexed customers' former supplier to access new suppliers to serve the annexed load." Order 888-B, ¶ 61,248 at 62,102. In such cases, FERC will determine on a case-by-case basis whether there exists the requisite nexus between municipal annexation and open access transmission. Recognizing that state regulatory authorities may be the first to address claims for stranded cost recovery in the retail-turned-wholesale scenario (FERC's label for new municipalizations and municipal annexations), FERC stated that it "will take into account state findings on cost determinations ... and will give great weight in [its] proceedings to a state's view of what might be recoverable." *Id.* At 62,105 (internal quotation marks omitted).

This issue provoked the only dissents to Order 888. Although neither dissenting commissioner disputed FERC's jurisdiction to allow recovery of these stranded costs, both faulted FERC for second-guessing state authorities regarding stranded costs. They thought that FERC should have acted as the forum for adjudicating these stranded cost issues only when state authorities failed to act altogether. *See* Order 888, ¶ 31,036 at 31,904-07 (Commissioner Hoecker concurring in part and dissenting in part); *id.* At 31,907 (Commissioner Massey dissenting in part).

Unlike the dissenters, both the States and POSCR challenge FERC's assertion of jurisdiction. According to the (82)States, FERC usurped their role as protectors of retail customers by

potentially undermining their rate treatment of retail costs. POSCR makes three arguments. Advancing claims similar to its arguments about stranded costs resulting from state-ordered retail wheeling (*see* Section V.B.1.a *supra*), POSCR first contends, relying again on section 201(b), that FERC lacks jurisdiction to award retail stranded costs in the retail-turned-wholesale scenario. Second, it claims, FERC failed to weigh properly the adverse effects of Order 888 on franchise competition between utilities and municipalities. Finally, relying on the Hoecker and Massey dissents, POSCR argues that FERC acted arbitrarily and capriciously by declaring itself to be the primary forum for retail-turned-wholesale stranded cost claims. For their part, the IOUs fault FERC's failure to consider claims for recovery in the so-called "bypass" scenario. We address these arguments in turn.

The States begin their argument by asserting that "[w]hen retail utility customers leave the utility's system because of municipalization, the costs stranded by the customers' migration normally are not allocable ... to whatever wholesale utility service *might* be sold to the city for resale." While this may have been true in the past, the States' argument ignores FERC's conclusion that it is open access transmission that makes municipalization feasible. Because FERC has determined that it will consider proposals for stranded cost recovery only when there is a direct nexus between municipalization and open access transmission, we see no basis for the States' claim that FERC will "override Congress's instruction that the states be permitted to protect retail customers."

The answer to POSCR's first argument—that section 201(b) precludes FERC from awarding stranded costs in the retail-turned-wholesale context—appears in our discussion of FERC's jurisdiction to address retail stranded costs resulting from state-ordered retail wheeling. *See* Section V.B.1.a *supra*. Because a town becomes a wholesale customer of the historic supplying

utility when it municipalizes, FERC's exclusive jurisdiction over all aspects of wholesale sales gives (83)FERC all the authority it needs to include generation-related costs in rates, including even costs originally incurred to provide retail service. We find no reason to question FERC's decision to allocate stranded costs caused by retail-turned-wholesale customers to the cost of providing wholesale service subject to its jurisdiction. As in the retail wheeling context, these stranded costs are properly viewed as "costs" of the former supplying utility's provision of open access transmission service. With respect to new municipalizations, the retail-turned-wholesale customer is able to reach a new generation supplier only because of open access transmission. And with respect to municipal annexations, FERC will require utilities to demonstrate a nexus between the annexation and open access transmission.

POSCR's second argument relates to what is known as "franchise competition." According to POSCR, franchise competition occurs "when a privately-owned utility is threatened by the prospect that a municipality may exercise powers of eminent domain to take over the utility's operations." POSCR argues that stranded cost recovery could impede franchise competition, which it says FERC has always encouraged. Although this might well be true, the possibility that potential stranded cost liability could deter municipalities from taking advantage of open access does not undermine Order 888. As Order 888-A explains, "the purpose of the stranded cost policy is neither to encourage nor to discourage municipalization, but rather to facilitate a fair transition to competition and to ensure stability in the industry during that transition." Order 888-A, ¶ 31,048 at 30,405.

We turn finally to POSCR's claim that FERC acted arbitrarily and capriciously by declaring itself the primary forum for recovery of retail-turned-wholesale stranded costs. Asserting that FERC's action implicitly undermines state decisionmaking and

encourages forum shopping, POSCR claims that Order 888's treatment of the retail-turned-wholesale scenario contravenes agency precedent and conflicts with the agency's decision to leave to the states the consideration of those stranded costs resulting from state-ordered wheeling.

(84)While FERC did leave resolution of claims for wholesale-turned-retail stranded costs to the states in *United Illuminating Co.*, 63 FERC ¶ 61,212 (1993), a pre-Order 888 case addressing a particular utility's application for stranded cost recovery, Order 888-A explains that, after reanalyzing the stranded cost problem, FERC concluded that "where such costs are stranded as a direct result of Commission-mandated wholesale transmission access, these costs should be viewed as costs of the transition to competitive wholesale bulk power markets and this Commission should be the primary forum for addressing their recovery." Order 888-A, ¶ 31,048 at 30,407. In our view, this explanation adequately distinguishes between recovery of stranded costs from retail customers and recovery from retail-turned-wholesale customers. In the former situation customers remain retail customers subject to state jurisdiction; in the latter situation, customers become wholesale customers subject to FERC's *exclusive* jurisdiction. This very different result justifies FERC's different treatment of the two situations.

The IOUs argue that FERC should have provided for stranded cost recovery from a retail-turned-wholesale customer who ceases to purchase power from a utility but does not use that utility's transmission service to reach another power supplier—the so-called "bypass" scenario. This argument requires little discussion. In declining to provide a mechanism for the recovery of bypass stranded costs, FERC explained that "Order No. 888 does not by its terms bar the recovery of costs that do not result from the use of Commission-required transmission access. Utilities may, as before, seek recovery of such non-open-access-related costs on a case-by-case basis in

individual rate proceedings. The Commission will not prejudge those issues here." *Id.* At 30,409. Given FERC's discretion to proceed through adjudication rather than by generic rule, *see SEC v. Chenery Corp.*, 332 U.S. 194, 201-03 (1947), the IOUs' challenge is without merit.

* * *

As evidenced by the numerous petitions for review, FERC faced an enormously difficult task in fashioning a stranded (85)cost recovery mechanism that fairly compensates utilities for past investments while transitioning the electricity industry to competition. FERC has done an admirable job. Producing a comprehensive, evenhanded record and carefully considering all commenters' claims, it adopted a stranded cost recovery policy that accomplishes its stated objectives, complies with the FPA, conforms to our case law, and reasonably accommodates all competing interests. No doubt, there were alternative approaches to stranded cost recovery—petitioners have pointed to several. No doubt some aspects of Order 888 could have been better supported. But given the extremely technical nature of these issues, as well as our highly deferential standard of review, we find no basis for questioning FERC's approach. Although Order 888 may be characterized in many ways, it can hardly be said to be either arbitrary or capricious.

VI. Credits for Customer-Owned Facilities and Behind-The-Meter Generation

The Commission's Open Access Tariff requires that public utilities—or "transmission providers"—offer "network integration transmission service." This requirement is one of the key elements in the Commission's attempt to "remove impediments to competition in the wholesale bulk power marketplace," Order 888, ¶ 31,036 at 31,634. Network service allows a customer—for instance, a municipal utility—to use a

transmission system in a manner comparable to the way the transmission provider utilizes its system to move power from its generators to its native load customers.[11] *See* Order 888, (86)¶ 31,036 at 31,736; *id.* At 31,751; Order 888-A, ¶ 31,048 at 30,260 n.247; *id.* At 30,325.[12] With network service, resources located throughout the system serve loads dispersed throughout the system. For this, the transmission provider incorporates the network customer's resources and loads (projected over a minimum ten-year period) into its own long term planning. Because network service ultimately provides the customer with the same full system ability for transmitting power as the transmission owner, the Commission required that costs be allocated on the basis of a ratio of the network customer's load to the transmission provider's entire load on its transmission system. A group of petitioners, led by Florida Municipal Power Agency (FMPA), challenge the Commission's use of this "load-ratio pricing."

The FMPA petitioners do not object to load-ratio pricing as such. In fact they think it "is a good method to allocate the costs of a transmission network among network owners or users,"

---

[11] "Load" may be defined as "[t[he total demand for service on a utility system at any given time." PUBLIC UTILITIES REPORTS GLOSSARY FOR UTILITY MANAGEMENT 84 (1992); *see also* CARL PECHMAN, REGULATING POWER: THE ECONOMICS OF ELECTRICITY IN THE INFORMATION AGE 11 (1993). The Tariff defines "native load customers" as the "wholesale and retail power customers of the Transmission Provider on whose behalf the Transmission Provider, by statute, franchise, regulatory requirement, or contract, has undertaken an obligation to construct and operate the Transmission Provider's system to meet the reliable electric needs of such customers." Order 888-A, ¶ 31,048 at 30,508.

[12] Public utilities must also offer point-to-point service, that is, transmission service reserved and/or scheduled between specified points of receipt and delivery. Order 888-A, ¶ 31,048 at 30,508.

Brief of Credits for Customer-Owned Facilities, etc., at 3-4 ("Credits Brief"). Their principal complaint, repeated many times and in many ways throughout their briefs, stems from their view that as a practical matter the commission required that the network customer's *total* load be used in calculating the ratio,[13] even though some customers "sell power from local, 'behind the meter' generation and transmission, or ... obtain power from more than one transmission system...." *Id.* At 8.[14] The FMPA petitioners say this (87)allows "transmission providers to charge wholesale customers for network transmission that they do not want, need or use to provide electric power service to their customers." *Id.* at 18.

The Commission provided some relief in response to these complaints, but not enough to satisfy the FMPA petitioners. "Because of the diverse concerns raised by the commenters," the Commission wrote in the preamble to Order No. 888, "we are unable to resolve on the basis of this record the extent to which, or under what circumstances, cost credits related to customer-owned facilities would be appropriate under an open-access transmission tariff." Order 888, ¶ 31,036 at 31,742. Rather, this will be done on a case-by-case basis. The Commission warned, however, that mere interconnection between a customer's facilities and the transmission provider's facilities will not be sufficient to warrant a cost credit. Relying on *Florida Municipal Power Agency v. Florida Power & Light Co.*, 67 F.E.R.C.

---

[13] The Commission did not actually require a customer to designate its total load to obtain network service: a customer may exclude all—not merely part—of its load at a discrete delivery point. *See* Order 888-A, ¶ 31,048 at 30,256-62.

[14] "Behind the meter generation [and transmission] means generation [or transmission] located on the customer's side of the point of delivery." Order 888-A, ¶ 31,048 at 30,254 n.230.

¶ 61,167 (1994) *(FMPA I)*, *modified*, 74 F.E.R.C. ¶ 61,006 (1996) *(FMPA II)*, the Commission required the customer to demonstrate that its "transmission facilities are integrated with the transmission system of the transmission provider" and "provide additional benefits to the transmission grid in terms of capability and reliability, and [are] relied upon for the coordinated operation of the grid." Order 888, ¶ 31,036 at 31,742; Order 888-A, ¶ 31,048 at 30,271. The Commission did, however, guarantee credits for new, integrated transmission facilities built by a customer if jointly planned with the transmission provider.

We detect nothing in the arguments of the FMPA petitioners to warrant setting aside this aspect of the Commission's rule. It is true that as the owners of generation and transmission facilities, any one of these petitioners can satisfy some of its needs. But network service, as the Commission defined it, means that network customers can call upon the transmission provider to supply not just some, but all of their load at any given moment, when for instance they experience blackouts or brownouts. The Commission decided that if a customer does not desire such full network service for its entire load, it may exclude loads at discrete delivery points (88)and purchase point-to-point service instead. What it cannot do is split loads at delivery points. The FMPA petitioners object to the Commission's refusal to allow a split system, but their objection is not well-taken. They ignore the technical problems with a split system, stemming partly from the manner in which electrons flow and the impossibility of isolating loads from the transmission provider's system. *See FPC v. Florida Power & Light*, 404 U.S. 453 (1972). Furthermore, "such a split system creates the potential for a customer to 'game the system' thereby evading some or all of its load-ratio cost responsibility for network services." Order

888-A, ¶ 31,048 at 30,259.[15] The FMPA petitioners label this prospect a "fiction," but offer neither evidence nor reasoning to counter the Commission's expert judgment.[16]

As to credits, these petitioners maintain that if the Commission is going to use total "load-ratio pricing with Network Load defined as total customer load, simultaneous credits are required." Credits Brief at 41. What they mean by credits is reduced prices for any and all behind-the-meter facilities they own. The Commission's rejection of this blanket approach is well-supported. Credit may be given, but not automatically. The question can only be determined on a case-by-case basis because it depends on whether the customer's facilities are truly integrated with the transmission system, rather than merely interconnected. Only if they are (89)integrated will the transmission system benefit and only then, the Commission decided, should credits—which shift the costs of the customer's facilities to the transmission provider's customers—be allowed. Order 888-A, ¶ 31,048 at 30,271. Petitioners call the Commission's rule in this regard "an unexplained and inexplicable retreat from *FMPA v. FPL*." Credits Brief at 42. It is nothing of the sort. The Commission made this abundantly clear. In *FMPA I* THE Commission said that "if [a customer] has transmission facilities that will operate as part of the integrated transmission

---

[15] Load-ratio cost responsibility is based on the customer's contribution to the transmission system peak each month. With a split system a customer could, at the time of the monthly system peak, increase its behind-the-meter generation in order to decrease its load-ratio cost responsibility, while making significant use of the transmission system throughout the rest of the month. *See* Order 888-A, ¶ 31,048 at 30,259 & nn.244 & 245.

[16] Petitioners claim that *Florida Power Co.*, 81 F.E.R.C. ¶ 61,247 (1997), decided after Order No. 888, shows that it is not "necessary for customers to purchase amounts of network transmission equal to their entire load behind a delivery point." Credits Brief at 30. It shows no such thing. The case involved not network integration transmission service, but a sort of hybrid service called "network contract demand transmission service."

system, a credit would be reasonable." 67 F.E.R.C. at 61,482 n.76. And in *FMPA II* the Commission said that mere interconnection does not equal integration and that integration must be determined case by case. 74 F.E.R.C. at 61,010. This is completely consistent with the Commission's resolution of the credits issue in the proceedings before us.

The FMPA petitioners' next objection deals with new customer facilities—that is, those built after network service begins under the Tariff. The Commission determined that "the Network customer shall receive a credit where such facilities are jointly planned and installed in coordination with the Transmission Provider." Order 888-A, ¶ 31,048 at 30,534. Petitioners begin by reading this as some sort of "limitation," they expand it into a "condition precedent for customers to receive credit for new facilities," and they end by treating it as a bar to "credits for new customer-facilities unless they are jointly planned," Credits Brief at 43, 44, 45. Commission counsel rightly points out that petitioners have completely misread the rule: "simply put, the Rule does not speak to the situation of new facilities built outside a joint planning effort." Commission Brief at 104. The Commission did determine that a joint planning mandate was "beyond the scope of this proceeding," Order 888-A, ¶ 1,048 at 30,311. Using their mistaken premise, petitioners insist that the Commission acted arbitrarily in this regard, giving transmission providers the power to block all customer credits for new facilities. *See* Credits Brief at 45. Since their premise is mistaken, their conclusion must be rejected. The balance of (90)the FMPA petitioners' arguments have been considered and rejected.

VII. LIABILITY, INTERFACE ALLOCATION, AND DISCOUNTING

As part of Order 888, FERC adopted a pro forma Open Access Transmission Tariff (OATT), containing minimum terms and conditions for non-discriminatory service, which every

transmission-owning public utility must file with the Commission and by which it must abide in providing transmission services to itself and others. Various petitioners have challenged isolated provisions of the OATT—specifically the provisions governing liability and indemnification, interface allocation, and delivery-oint specific discounting. We reject each of these challenges.

A. *Liability and Indemnification*

Prior to unbundling, retail tariffs were primarily a matter for state regulation, and most states had approved tariff provisions permitting utilities to limit their liability for service interruptions to instances of gross negligence or willful misconduct. Courts upheld these limitations on the public policy grounds that they balanced lower rates for all customers against the burden of limited recovery for some, and that the technological complexity of modern utility systems and resulting potential for service failures unrelated to human errors justified liability limitations. In the past, FERC also has allowed electric utility tariffs to explicitly limit a utility's liability for service interruptions to instances of gross negligence or willful misconduct.

One of the pro forma tariffs included in the Notice of Proposed Rulemaking contained a provision explicitly limiting the liability of transmission providers to circumstances of gross negligence or intentional wrongdoing. *See* Open Access NOPR, ¶ 32,514 at App. C § 15.0. Section 10.2 of the OATT requires the transmission customer to "at all times indemnify, defend, and save the Transmission Provider harmless from, any and all damages ... except in cases of *negligence* or intentional wrongdoing by the Transmission Provider." Order 888, ¶ 31,036 at 31,936-37 (emphasis added). In Order (91)888, FERC justified the change with a single statement: "We find that this new indemnification provision would be too strict if it required customers to indemnify transmission providers even in cases

where the transmission provider is negligent." Order 888, ¶ 31,036 at 31,765.

The investor owned utility petitioners (IOUs) challenge the OATT's indemnification provision on the ground that FERC adopted the lesser ordinary negligence standard in Order 888 without first notifying interested parties that it was contemplating such a major policy change The IOUs claim that the change in the provision's language represents a significant shift in indemnification policy, in that it leaves transmission providers open to claims of ordinary negligence for the first time. The courts consistently have relied upon explicit tariff provisions to enforce the gross negligence standard for liability, *see, e.g., Southwestern Bell Tel. Co. v. Rucker*, 537 S.W.2d 326, 330-32, 334 (Tex. App. 1976); and if the tariffs do not explicitly limit liability for ordinary negligence, the IOUs claim, the courts will assess such matters differently. Because FERC's notice was not clear that the liability standard was a subject or issue of the rulemaking, the IOUs claim that FERC denied their right to comment on the change. *See, e.g., AFL-CIO v. Donovan*, 757 F.2d 330 (D.C. Cir. 1985); *McLouth Steel Prods. Corp. v. Thomas*, 838 F.2d 1317 (D.C. Cir. 1988). Citing principally our opinion in *Air Transport Association of America v. DOT*, 900 F.2d 369, 379 (D.C. Cir. 1990), the IOUs contend that the fact that they were able to raise their concerns in their petition for rehearing is not a substitute for pre-issuance notice and comment.[17]

FERC responds by denying that the indemnification provision adopts a particular liability standard at all. FERC claims that it has merely distinguished liability from indemnification, and that the change to the pro forma tariff does not establish a new,

---

[17] We recognize that *Air Transport* has been vacated. *See Air Transport Association of America v. DOT*, 933 F.2d 1043 (1991) (per curiam).

simple negligence standard of liability for transmission providers. Citing its own statements in Order (92)888-A, FERC asserts that the tariff's indemnification provision should not be construed as preempting state liability standards. *See* Order 888-B, ¶ 61,248 at 62,080-81. FERC maintains that, since the change to the indemnification provision does not represent a substantive alteration in policy or the standards governing legal liability, the Commission was not obligated to notify interested parties and seek comment. FERC accuses the petitioners of wanting FERC to impose a federal gross negligence liability standard, which FERC contends that it properly declined to do pursuant to *United Gas Pipe Line Co. v. FERC*, 824 F.2d 417 (5th Cir. 1987) (rejecting the need for a federal liability standard for pipelines).

The IOUs charged that FERC has deleted a limitation of liability to gross negligence from the existing background of utilities liability law and has done so without substantial evidence and without exercising reasoned decision making. *See Mid-Tex Elec. Coop., Inc. v. FERC*, 773 F.2d 327, 338 (D.C. Cir. 1985) (the Commission's decision must be supported by substantial evidence and be the result of reasoned decision making). The Commission denies that it has established a standard of liability nearly so sweeping as the IOUs fear. We agree with FERC's reading of the rule. While the petitioners argue that the rule works a "dramatic change" regarding the liability of electric utilities by imposing an ordinary negligence rather than a gross negligence standard that previously prevailed, in fact, the rule does not establish a new simple negligence standard of liability for transmission providers. While we read FERC's interpretation of its own rule deferentially, *see Jersey Shore Broad. Corp. v. FERC*, 37 F.3d 1531, 1536 (D.C. Cir. 1994), by any standard, its construction is correct in the present controversy. In the preamble to the regulations before us, FERC plainly describes the disputed provision as an "indemnification" provision, and recites reasoning supporting the particular indemnification

provision it adopted. "[T]his new indemnification provision would be too strict if it required customers to indemnify transmission providers even in cases where the transmission provider is negligent." Order 888, ¶ 31,036 at 31,765. In the preamble to Order 888-A, in a section concededly headed "*Liability* and Indemnification" (emphasis added), FERC explains the later version of the relevant provisions in terms consistent with the Order 888 preamble. *See generally* Order 888-A, ¶ 31,048 at 30,299-302. Finally, in Order 888-B, FERC summarizes its reasoning for its indemnification and liability decisions, again both adequately and in ways not amounting to the adoption of the universal standard as asserted by the IOUs. *See generally* Order 888-B, ¶ 51,248 at 62,079-81. In short, FERC's rule does not work so sweeping a change in the legal landscape as the IOUs assert, and FERC has exercised reasoned decisionmaking in support of such pronouncements as it has made.

Insofar as the IOUs challenge the adequacy of FERC's notice in the NOPR that it was contemplating a change in the indemnification and liability provisions of pro forma tariffs, that challenge also fails. It is well established that a final rule need not be identical to the original proposed rule. *See, e.g., AFL-CIO v. Donovan*, 757 F.2d at 338; *Trans-Pacific Freight Conference v. Federal Maritime Comm'n*, 650 F.2d 1235, 1249 (D.C. Cir. 1980). Were the change between the proposed and final rule an important one, we would have to ask whether the final rule is a logical outgrowth of the proposed one. *See, e.g., National Mining Ass'n v. Mine Safety & Health Admin.*, 116 F.3d 520, 531 (D.C. Cir. 1997). Not all changes are sufficiently important to warrant such scrutiny and concern, however. "An agency, after all, must be free to adopt a final rule not described exactly in the [notice of proposed rulemaking] where the difference is sufficiently minor, or agencies could not change a rule in response to valid comments without beginning the rulemaking

anew." *National Cable Television Ass'n v. FCC*, 747 F.2d 1503, 1507 (D.C. Cir. 1984).

We agree with FERC that its indemnification provision does not preclude the states from shielding utilities from liability for ordinary negligence. States did so before, through both their regulatory commissions and their courts; and they remain free to do so under Order 888. The deletion of the gross negligence language from the pro forma tariff's indemnification provision does not significantly change the (94)petitioners' legal position. Therefore, contrary to the IOUs' challenge, the deviation of the final rule from the proposed one is not a major one; and FERC's failure to notify interested parties that it was considering the change does not render the provision arbitrary or capricious under the APA. Accordingly, we affirm this portion of the pro forma tariff.

B. *Interface Allocation*

The IOUs also challenge FERC's treatment of interface allocation as unsupported by the record and contrary to reasoned decision making. Section 30.8 of the pro forma tariff addresses how much of a transmission provider's interface capacity a network customer can use. *See* Order 888, ¶ 31,036 at 31,954-55. Interface capacity represents the capability of a transmission facility to transfer power between two utilities. Section 30.8 permits a network customer to use a transmission provider's capacity to the extent of the network customer's total load without limitation.

In the rulemaking process, several parties argued that a fair method of interface allocation would be the use of a load ratio, under which the transmission provider and each network customer would be allocated a share of each specific interface based upon their respective loads. Nevertheless, in Order 888, FERC ruled that network customers could use any of the

transmission providers' interfaces to import up to their full load on a first-come, first-served basis. The IOUs maintain that this ruling does not promote an equitable allocation of a transmission provider's interfaces.

The IOUs also note that, responding to the IOUs petition for rehearing on this issue in Order 888-A, FERC merely referenced *Florida Municipal Power Agency v. Florida Power & Light Co.*, 74 F.E.R.C. ¶ 61,006 (1996) (hereinafter *FMPA II*), to support its conclusion, without addressing either the comments or the rehearing petitions. FERC meanwhile maintains it found the load ratio share method advocated by some transmission owners to be unreasonable for the same reasons discussed at length in *FMPA II*. Intervenors add that the IOUs' challenge of the aggregate, (95)first-come, first-served approach adopted by FERC as inequitable merely reflects a disagreement with FERC's policy choice.

Whether to adopt a load ratio share approach or an aggregate, first-come, first-served approach to capacity allocation is a matter of policy. Again, the IOUs have not challenged FERC's legal authority to select a particular interface allocation method, but rather whether FERC's choice was based upon reasoned decision making. Accordingly, we evaluate FERC's treatment of interface capacity allocation under the APA's arbitrary and capricious standard. *See* 5 U.S.C. § 706(2)(A) (1994).

FERC's analysis of the issue in the present rulemaking consists solely of a reference to and quotation from its earlier decision in *FMPA II*. *See* Order 888-A, ¶ 31,048 at 30,304-05. That proceeding involved an application by Florida Municipal Power Agency for open access to Florida Power & Light Company's transmission facilities pursuant to FPA §§ 211 and 212. *See FMPA II*, 74 F.E.R.C. ¶ 61,006 at 61,004; *see also Florida Mun. Power Agency v. Florida Power & Light Co.*, 67

F.E.R.C. ¶ 61,167 (1994) (hereinafter *FMPA I*). In *FMPA I* and *FMPA II*, FERC justified its choice of policies as follows:

> [T]here are no restrictions on the use of other parts of the transmission system. If the interfaces are constrained, Florida Power and FMPA should simply redispatch and share the redispatch costs and, ultimately, Florida Power will build new facilities when needed. The interfaces are just another part of the transmission grid, and Florida Power must plan and operate the grid, including the interfaces, to meet the combined needs of Florida Power and FMPA on an equal basis. When there are conflicting needs to use the same interface capacity, the parties have already agreed that the combined Florida Power and FMPA systems will be redispatched and the costs shared. When the grid, including interfaces, needs to be expanded, Florida Power will undertake the expansion on behalf of the combined system.

(96)*FMPA II*, 74 F.E.R.C. ¶ 61,006 at 61,018 (quoting *FMPA I*, 67 F.E.R.C. ¶ 61,167 and 61,484. While FERC's recognition of the petitioner's concerns was certainly cursory, and its language in *FMPA II* is slightly oblique, FERC has adequately demonstrated that it gave full consideration before rejecting load ratio share in favor of aggregate, first-come, first-served capacity allocation. Accordingly, we uphold FERC's ruling on the interface capacity allocation issue.

C. *Delivery-Point-Specific Discounting*

Two groups of transmission dependent utilities, TAPS and TDU Systems, and the nation's largest power wholesaler, Enron Power Marketing (collectively the U&D petitioners), challenge FERC's decision to permit delivery-point-specific discounting.

Electric utilities often offer both firm and non-firm service. Firm service permits customers to demand transmission at any time, while non-firm service permits the utility to cut service when there is not enough excess capacity.

In Order 888, FERC allowed transmission providers to offer discounted rates for non-firm service only if they gave the same discounted rate to all customers for the same transmission path and on all other unconstrained transmission paths. *See* Order 888, ¶ 31,036 at 31,743-44. FERC also required that the discounts be posted in advance so that all customers could have equal opportunity to take advantage of the discounted rate. *See id.* at 31,744. In Order 888-A, FERC narrowed the requirement, so that a transmission provider offering a discount on a particular path need only provide the same discount to all other unconstrained paths that go to the same delivery point in the provider's system. *See* Order 888-A, ¶ 31,048 at 30,275-76. FERC also said that a transmission provider should discount only if necessary to increase throughput on its system. *See id.* at 30,274.

The U&D petitioners contend that delivery-point-specific discounting results in higher transmission rates for transmission dependent utilities (TDUs), who rely on point-to-point service rather than network service for their transmis(97)sions. Delivery-point-specific discounting permits transmission facility owners to select the delivery points for which they will discount firm and non-firm service. The U&D petitioners argue that this discounting method allows transmission facility owners to discriminate by denying discounts to the delivery points used by the TDUs, thereby raising the transmission costs of these competitors, and in turn decreasing competition at both retail and wholesale.

Additionally, because of the subordination and interruptibility of non-firm service, the U&D petitioners claim that FERC's

longstanding pricing policies utilized discounting as the mechanism for ensuring that non-firm service was priced below firm service. The notice of proposed rulemaking emphasized FERC's reliance on non-discriminatory discounting to achieve higher firm service rates than non-firm rates, so that non-firm rates would reflect the interruptibility of transmission services and be economically efficient. The petitioners argue that FERC's decision in Order 888 to deny discounting of non-firm rates unless firm rates are also discounted an unexplained reversal of that longstanding pricing policy. By adopting a deliver-point-specific discounting rule, the petitioners claim that FERC subjects TDUs to firm rates for all non-firm service. As a result, the petitioners contend, the price that TDUs have to pay for non-firm service does not reflect the interruptibility of that service. The petitioners maintain that this aspect of FERC's order itself represents undue discrimination, and that FERC failed to explain why it rejected a compromise position which would restrict opportunities for discrimination and address concerns that the new rules discourage discounting.

FERC notes that it discussed the discounting issue in Orders No. 888, 888-A, and 888-B. *See* Order 888, ¶ 31,036 at 31,743-44; Order 888-A, ¶ 31,048 at 30,272-76; Order 888-B, ¶ 61,248 at 62,072-75. FERC accuses the petitioners of wanting the Commission to require transmission providers to discount all non-firm services below firm rates regardless of the facts of the particular case. FERC asserts that it did not seek to discourage discounting, but was concerned that if it required discounting on all unconstrained paths as a condition (98)for offering discounts, transmission providers would be discouraged from offering any discounts at all. Fewer discounts could lead to decreased use of transmission services, and therefore a decline in overall transmission revenues, and a corresponding increase in transmission rates to enable transmission providers to recover their costs. FERC maintains that the petitioners, like everyone else, retain the opportunity to compete with the transmission

provider for power sales to the same delivery point at the same discounted rate. FERC argues that its orders are consistent with its established pricing policy of permitting flexibility to reflect interruptibility and efficient use of the transmission system, subject to the firm price cap. In most case, FERC expects that non-firm transmission rates will be priced below the firm rate.

Although the petitioners hint at a statutory claim by alleging that FERC's orders result in undue discrimination and higher rates in violation of the FPA's statutory mandate, the petitioners generally confine themselves to arguing that FERC's decisions to permit delivery-point-specific discounting and non-firm rates equal to firm rates represent unexplained departures from established policy. We therefore analyze this issue under the arbitrary and capricious standard of the APA. *See* 5 U.S.C. § 706(2)(A).

With respect to non-firm versus firm rates, the cases cited by the petitioners as demonstrating a previously established discounting policy actually establish that FERC addresses this issue on a case-by-case basis. For example, in *Kentucky Utilities Co.*, 15 F.E.R.C. ¶ 61,002 (1981), FERC said that the utility could not allocate capacity costs to non-firm transmission service since such service did not factor into the utility's capacity decisions. In contrast, in *Central Maine Power Co.*, 60 F.E.R.C. ¶ 61,285 (1992), while FERC noted that non-firm service generally warrants a rate lower than firm service, FERC also upheld the utility's decision not to offer non-firm rate discounts on several contracts. Indeed, the petitioners acknowledge that FERC's pre-Order 888 Transmission Pricing Policy Statement, 59 Fed. Reg. 55,031 (1994), does not (99)expressly require non-firm rates to be priced below firm rates in all cases. *See* Br. of U&D Petitioners at 24 n.30.

The petitioners cite *American Electric Power Service Corp.*, 82 F.E.R.C. ¶ 61,090 (1998), for the proposition that, after

adopting delivery-point-specific discounting, FERC has refused to consider whether non-firm rates should be lower than firm rates; but in that case, FERC did consider that issue, found the rates in question to be nondiscriminatory, and refused only to consider the petitioners' generic challenges to its broader policy of flexibility. Additionally, the petitioners charge that FERC's acceptance of firm rates for non-firm service conflicts with this court's decision in *Fort Pierce Utilities Authority v. FERC*, 730 F.2d 778, 788-89 (D.C. Cir. 1984); but in that case, this court merely noted that FERC had failed to reconcile its decision to allocate capacity costs to non-firm transmission service with its previous refusal to do so in *Kentucky Utilities*, and remanded for further consideration. In short, FERC does not appear to have changed its overall pricing policy at all, except to fine tune its guidance as to when discounting might be considered discriminatory.

Which brings us to whether delivery-point-specific discounting in fact discriminates against the TDUs. Essentially, FERC and the petitioners offer conflicting discounting theories, both of which seem plausible. In its request for rehearing, TAPS observed that, by allowing transmission providers to select which delivery points merit discounts, FERC permits the providers to select for discounting those delivery points which serve their affiliates, and not to select the similarly situated delivery points which serve the TDUs. On rehearing, FERC quite logically maintained that requiring transmission providers to apply discounts to all unconstrained transmission paths could discourage discounting generally, resulting in higher rates for all. *See* Order 888-A, ¶ 31,048 at 30,275. FERC subsequently asserted that requiring transmission providers to offer the same discount for the same time period on all unconstrained paths that go to the same (100)delivery point will achieve sufficient comparability. *See* Order 888-B, ¶ 61,248 at 62,075. FERC noted that it will be able to monitor the discounting behavior of

transmission providers for discrimination through the data posted on OASIS. *See id.*

The record reflects that FERC considered fully all of the arguments, and concluded that delivery-point-specific discounting best accomplished comparability while encouraging discounting. Thus, the discounting policies outlined in Orders 888, 888-A, and 888-B are not arbitrary or capricious. We therefore affirm FERC's resolution of this issue.

VIII. TARIFF TERMS AND CONDITIONS

A. *Headroom Allocation*

Firm point-to-point service, as distinguished from network service, is transmission service reserved and/or scheduled between specified points of receipt and delivery. *See* Order 888-A, ¶ 31,048 at 30,508. Point-to-point customers may not need all the service for which they contracted. The Commission decided that they may, without extra charge, use their excess capacity to make firm sales between the receipt and delivery points specified in their agreement. Section 22.1 of the Tariff gives them another option for dealing with this "headroom." The point-to-point customer may, without charge, have the public utility provide transmission on a non-firm basis over receipt and delivery points other than those specified in the service agreement (so-called "secondary" points).

Network customers describing themselves as Transmission Dependent Utilities (TDUs) contend that the flexibility given to point-to-point customers to sell their unused capacity should also be given to them. Three transmission providers[18]—the CPL

[18] Carolina Power & Light Company (CPL), Florida Power & Light Company and Niagara Mohawk Power Corporation.

petitioners—want restrictions placed on point-to-(101)point customers in order to avoid putting the customers at a competitive advantage. The Commission refused to adopt these proposals for reasons we believe are sound.

As to transmission providers, the Commission noted that if they want to make off-system sales they too must take point-to-point service; in doing so they gain the same flexibility as regular point-to-point customers. *See* Order 888, ¶ 31,036 at 31,751. For network customers, the Commission stated that they "are not obligated to take network transmission service" and if they "want to take advantage of the as-available, non-firm service over secondary points of receipt and delivery through the point-to-point service, they may elect to take firm point-to-point transmission service in lieu of the network service." Order 888-A, ¶ 31,048 at 30,253. The Commission properly insisted on maintaining its basic distinctions between network service and point-to-point service. Unlike a point-to-point customer, a network customer's rights are defined in terms of capacity needed, and thus "vary as the customer's load varies," rendering them not sufficiently definite and defined to be "reassignable in the secondary market." *Id.* at 30,223. At least one of the TDUs agreed with the Commission "that, because there is no fixed capacity reservation for network customers, allowing them unrestricted use of capacity to make off-system sales without additional charge would give such customers a competitive advantage over [point-to-point] customers." Terms and Conditions Brief at 11.[19]

[19] These petitioners add that the Vermont Department of Public Service (VDPS) offered a solution to the problem but the Commission overlooked it. Terms and Conditions Brief at 12. This is not correct. The Commission did consider the Vermont proposal, finding it to be an "artifice derived from the load ratio share calculation," a "formula [that] does not result in a reassignable capacity right." Order 888-A, ¶ 31,048 at 30,223.

B. *Headroom Prioritization*

Some petitioners complain that secondary non-firm point-to-point customers should not have been placed in a status below non-firm point-to-point customers and that the Com-(102)mission offered no explanation for its doing so. *See* Terms and Conditions Brief at 14-17. The Commission did explain itself. Firm point-to-point customers are permitted to designate secondary receipt and delivery points at no extra charge and therefore "are properly accorded a lower priority than stand alone, non-firm transmission." Order 888-A, ¶ 31,048 at 30,281. Furthermore, the Commission promised to reevaluate its approach in response to any "future transmission rate proposal that is based on the concept of tradable capacity rights," but it was moving cautiously because in the electric utility industry (unlike the natural gas industry) such "trading rights simply do not exist at this time." *Id.*

C. *Duplicative Charges*

The TDU petitioners argue that the new rules cause them to be double-charged in certain transactions. They first object to the Commission's decision that in power exchanges (flows in one direction for a time and then flows in the opposite direction) each party must reserve and pay for transmission along the same path. *See* Terms and Conditions Brief at 18. The Commission's response was that traditionally and "from the transmitting utility's planning and reservation perspective," the power exchange consists of two one-way transmission services. Commission Brief at 115. Petitioners offer no legal basis for us to prefer their treatment to that of the agency and so we will not disturb the Commission's approach.

Petitioners' second objection is that the Tariff double counts network load served by two separate energy suppliers because, "[i]f two separate suppliers purchase network service to supply

a portion of the load for a particular customer, the entire load of the customer is included in calculating the reservation charges paid by both supplying network customers, unless each load portion is isolated electrically from the other." Terms and Conditions Brief at 21. We confess to some difficulty in comprehending petitioners' complaint. It seems perfectly reasonable to answer, as the Commission's counsel does, that "there is no rational basis for both the network transmission customer and its power marketer sup-(103)plier to designate the same load under the Tariff." Commission Brief at 115. The power supplier itself may, the Commission pointed out, purchase network service; we cannot see why both the power supplier and the power buyer would purchase such service when a purchase by either would suffice. Petitioners seem to concede that in some instances the double-counting problem could be avoided in this manner, yet they think that in some other, ill-defined circumstance it could not. This rulemaking set forth the standard tariff terms. If petitioners, or any one of them, have some unique circumstances warranting an adjustment, there will be time enough for them to seek relief from the Commission.

D. *Multiple Control Areas*

Network customers may wish to serve loads in two or more control areas. Some commenters were concerned that such customers would have to pay a network transmission rate to two or more transmission providers based on the customer's total load. *See supra* Section VI (credits for customers). The Commission had several responses. First, the risk could be avoided or alleviated by the customer's purchasing point-to-point service, or a combination of network and point-to-point service at discrete delivery points (thereby reducing its load ratio). Or the customer could purchase network service alone in each transmission provider's control area. *See* Order 888-B, ¶ 61,248 at 62,096 n.157. If the customer insists on foregoing the last option, it can hardly expect that the additional service it is

demanding—the moving of power from one transmission provider's system to another system—should be free of charge. As the Commission put it:

> Because the additional transmission service to non-designated network load outside of the transmission provider's control area is a service for which the transmission provider must separately plan and operate its system beyond what is required to provide service to the customer's designated network load [within the control area], it is appropriate to have an additional charge associated with the additional [point-to-point] service.

(104)Order 888-A, ¶ 31,048 at 30,255, *quoted in* Order 888-B, 81 F.E.R.C. ¶ 61,248 at 62,096. This is consistent with the handling of an analogous situation involving separate transmission systems in the past. *See Fort Pierce Utils. Auth. v. FERC*, 730 F.2d 778, 781-85 (D.C. Cir. 1984).[20]

E. *Right-of-First-Refusal*

In order to preserve the certainty and continuity of transmission service, the Commission granted existing customers a right-of-first-refusal (ROFR) upon the expiration of firm contracts exceeding one year provided that the existing customer agreed to match the contract price and term of any party competing for that service. *See* Order 888, ¶ 31,036 at 31,665. The Commission did not set an upper limit on the terms that a

[20] Petitioners claim that the Commission failed to consider a particular proposal related to this subject. *See* Terms and Conditions Brief at 33. It is unnecessary to describe the proposal. All that need be said is that the Commission rejected a nearly identical proposal and gave its reasons for doing so. *See* Order 888-B, ¶ 61,248 at 62,096.

competing party could offer, but chose instead to allow the market to determine rates and terms. Petitioners argue that the Commission's failure to establish an upper limit should be set aside and remanded for further consideration. The Commission conceded error on this point at oral argument in light of *United Gas Distribution Cos. v. FERC*, 88 F.3d 1105, 1138-40 (D.C. Cir. 1996). We therefore remand this matter to the Commission so that it may provide a reasonable cap on contract extensions.[21]

(105)IX. NATIONAL ENVIRONMENTAL POLICY ACT AND REGULATORY FLEXIBILITY ACT COMPLIANCE

A. *NEPA Compliance*

One investor-owned utility, Public Service Electric & Gas Company ("PSE&G"), claims that FERC failed to comply with the National Environmental Policy Act ("NEPA"), 42 U.S.C. §§ 4321 *et seq.* It argues first that the base case FERC adopted to evaluate the effects of open access transmission was unreasonable because it "defined away" the effects of open access. Second, it argues, FERC acted arbitrarily and capriciously by failing to undertake measures to mitigate the environmental impact of Order 888.

1. *Adequacy of Base Case*

NEPA requires federal agencies contemplating a major action "significantly affecting the quality of the human environment" to

[21] The TDU petitioners stated in their reply brief that Commission counsel's explanation of § 13.2 of the Tariff, as amended in Order No. 888-A and as interpreted in *Madison Gas & Electric Co.*, 82 F.E.R.C. ¶ 61,099 at 61,372 (1998), to apply only to short term customers satisfies their objection. *See* Terms and Conditions Reply Brief at 25. The remaining arguments of these petitioners not discussed in this part or in part V have been considered and rejected.

prepare a thorough analysis of the action's environmental impact. 42 U.S.C. § 4332(C). The statute requires that environmental impact studies include "a detailed statement ... [of] alternatives to the proposed action." *Id.* § 4332(C)(iii).

In its environmental impact study prepared in connection with Order 888, FERC identified as the base case alternative a scenario that "maintains] the status quo." FERC Final Environmental Impact Statement, *Promoting Wholesale Competition through Open Access Non-discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities* at 2-1 (Apr. 1996) ("*FEIS*") Under that scenario, FERC would continue on a case-by-case basis to (1) condition approval of mergers and applications for sales at market rates on the filing of open access tariffs and (2) approve open access wheeling orders under section 211 of the FPA. *Id.*

Several commenters (including EPA) argued that FERC should adopt as its base case an alternative that freezes the status quo, *i.e.*, assumes that no further open access transmission of any kind occurs and that efficiency in the industry remains unchanged. *See id.* at 6-1. Characterizing this (106)"frozen efficiency" case as unreasonable, FERC declined to adopt it as the base case. *See id.* at 6-9-6-14. It nevertheless conducted sensitivity analyses comparing emissions under the frozen efficiency case with those under its base case. This comparison revealed "modest" reductions in emissions under the frozen efficiency case in certain circumstances. *Id.* at 6-4. When market conditions favor coal versus natural gas, NO_x emissions under the base case are higher than under the frozen efficiency case by two percent in 2000, three percent in 2005, and five percent in 2010. *Id.* at 6-15. But when market conditions favor gas, the base case produces more favorable environmental benefits for all three years. *Id.* at 6-17.

We evaluate agency compliance with NEPA under a rule of reason standard. "[A]s long as the agency's decision is 'fully informed' and 'well-considered,' it is entitled to judicial deference and a reviewing court should not substitute its own policy judgment." *Natural Resources Defense Council, Inc. v. Hodel*, 865 F.2d 288, 294 (D.C. Cir. 1988) (quoting *North Slope Borough v. Andrus*, 642 F.2d 589, 599 (D.C. Cir. 1980)).

PSE&G argues that FERC, in adopting its base case, "defined away" the impact of open access by comparing the environmental effects that would result from immediate implementation through Order 888 to those that would result from gradual implementation. Calling FERC's evaluation of the frozen efficiency case "cursory," PSE&G contends that the proper no action base case is not to implement open access at all.

Given the terms of NEPA and our highly deferential review, we think FERC's FEIS complied with the statute. For one thing, NEPA does not require that a certain alternative be adopted as the base case. Rather, NEPA requires that agencies include in their FEIS analysis of "alternatives to the proposed action." 42 U.S.C. § 4332(C)(iii). Thus there is no merit to the contention that NEPA requires FERC to adopt the frozen efficiency case as the base case. We agree with PSE&G that one of the alternatives NEPA requires FERC to consider is the alternative of no action. (107)But based on our own examination of the FEIS, we think that FERC devoted sufficient attention to evaluating the frozen efficiency case (what PSE&G calls the no action alternative) to satisfy NEPA's requirements. In conducting sensitivity analyses to its base case, FERC identified the changes in both NO_x and CO_2 emissions that the frozen efficiency case would produce. Given that FERC's comparison of the frozen efficiency case to its base case yielded little difference, the agency had no reason to conduct further analysis. By rigorously examining the frozen efficiency case, even though it believed the case to be

unreasonable, FERC ensured that its decision was "fully informed" and "well-considered." *Hodel*, 865 F.2d at 294.

2. *Failure to Adopt Mitigation Measures*

PSE&G argues that FERC acted arbitrarily and capriciously by failing to adopt measures to mitigate the expected harmful environmental effects of Order 888. Noting that an agency must consider mitigation if the proposed action would result in adverse environmental impacts, FERC considered but ultimately rejected any mitigation measures. *See FEIS* § 7. In reaching this conclusion, FERC relied on (1) the fact that any mitigation measures it might undertake are unwarranted in view of Order 888's small impact (especially given that its effects are as likely to be beneficial as harmful) and (2) its lack of expertise in atmospheric chemistry, together with the fact that any impact of open access would be "dwarfed by the far larger existing ozone and NO_x emission issues" currently being dealt with by EPA under its Clear Air Act authority. *FEIS* at 7-47-7-48.

The heart of PSE&G's challenge is this: downwind utilities, which are subject to NO_x reduction requirements, will face increased compliance costs due to the purported increase in emission levels resulting from Order 888; by comparison, upwind utilities that generate the pollution but are not subject to NO_x reduction requirements will experience no increased costs. PSE&G insists that FERC remedy this "undue preference" for upwind utilities.

(108)Given that FERC has identified only small increases in emissions resulting from open access transmission—indeed, under some circumstances, the Commission predicted small decreases—we think it was entirely reasonable for FERC to decline to adopt mitigation measures to address a problem that it believed might not even develop. Not relying solely on Order 888's relatively insignificant environmental impact, however,

FERC comprehensively analyzed proposed mitigation measures, explaining why it declined to require any. In light of this thorough analysis, we think FERC's conclusion—that NO_x emission increases resulting from Order 888, if any, are best addressed by EPA and the states through a comprehensive emissions control program—is hardly arbitrary or capricious. We therefore have no need to resolve the parties' debate about FERC's legal authority to order environmental mitigation.

PSE&G also argues that FERC employed unreasonable assumptions in the FEIS and ignored its own data showing adverse environmental impacts. In our view, these arguments amount to an effort by PSE&G to substitute its own analysis for FERC's. To prevail in this court, it must demonstrate that FERC's analysis is arbitrary and capricious, a showing it has fallen far short of making.

B. *Regulatory Flexibility Act Compliance*

The Regulatory Flexibility Act requires agencies to conduct a regulatory flexibility analysis for any final rule. The Act exempts agencies from this requirement if they certify that "the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities." 5 U.S.C. § 605(a)-(b). Invoking this exemption, FERC certified that both Order 888 (open access) and Order 889 (OASIS and standard of conduct rules) would have no such impact. Order 888, ¶ 31,036 at 31,896; Order 889, ¶ 31,035 at 31,628.

The TDU petitioners claim that FERC failed adequately to consider the impact of Orders 888 and 889 on nonjurisdictional entities that may have to provide open access transmission and file open access tariffs under the orders' reciprocity provisions. In contrast to jurisdictional utilities, several non-(109)jurisdictional utilities are classified as small entities. According to TDU petitioners, the orders impose a significant

economic burden on them, requiring compliance activities as well as alterations to their operations.

Although the RFA's judicial review provision was amended in 1996, *see* Small Business Regulatory Enforcement Fairness Act, Pub. L. No. 104-121, tit. II, 110 Stat. 857 (1996), the TDU petitioners and FERC agree that the pre-amendment version of the RFA applies in this case. Under that version, our review is quite narrow. Section 611(b) provided that "[a]ny regulatory flexibility analysis ... and the compliance or noncompliance of the agency with the provisions of this chapter shall not be subject to judicial review. When an action for judicial review of a rule is instituted, any regulatory flexibility analysis for such rule shall constitute part of the whole record of agency action in connection with the review." 5 U.S.C. § 611(b) (1994). We have interpreted this language to mean that "'a reviewing court should consider the regulatory flexibility analysis as part of its overall judgment whether a rule is reasonable and may, in an appropriate case, strike down a rule because of a defect in the flexibility analysis.' We emphasize[ ], however, that 'a major error in the regulatory flexibility analysis may be, but does not have to be, grounds for overturning a rule.'" *Mid-Tex Elec. Co-op, Inc. v. FERC*, 773 F.2d 327, 340-41 (D.C. Cir. 1985) (quoting *Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 537-39 (D.C. Cir. 1983)).

In this case, FERC explained that Orders 888 and 889, considered in their entirety, do not have a "significant" impact on a "substantial" number of small entities. According to FERC, the orders will affect nonjurisdictional utilities only in the limited situation where they take advantage of a jurisdictional utility's open access transmission tariff. Given our highly deferential standard of review, and given the fact that petitioners have offered nothing other than their own views to the contrary, we have no basis for questioning FERC's judgment.

(110)FERC, moreover, was not insensitive to the potential impact of Order 888 on small nonjurisdictional entities. Order 888 contains a waiver provision allowing these entities to seek an exemption from compliance with the reciprocity conditions. *See* 18 C.F.R. § 35.28(e)(2) (allowing nonjurisdictional utilities to file a request for waiver "for good cause shown"). As of March 1997, FERC had granted waivers to thirty-six small entities. *See* Order 888-A, ¶ 31,049 at 30,578.

Most important in view of our standard of review, nothing in petitioners' arguments causes us to question the reasonableness of the reciprocity provisions themselves. *See Mid-Tex*, 773 F.2d at 340-41. We therefore affirm FERC's RFA certification.

CONCLUSION

In summary, we affirm Orders 888 and 889 in all respects except as specifically provided above.

APPENDIX D

Section 31,036 Federal Energy Regulatory Commission Regulations Preambles (Order 888)

[¶31,036]

61 F.R. 21540 (May 10,1996)
18 CFR Parts 35 and 385
[Docket Nos. RM95-8-000 and RM94-7-001; Order No 888]

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities.

Issued April 24, 1996

AGENCY: Federal Energy Regulatory Commission, DOE.

ACTION: Final rule.

SUMMARY: The Federal Energy Regulatory Commission (Commission) is issuing a Final Rule requiring all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce to have on file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service. The Final Rule also permits public utilities and transmitting utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and Federal Power Act section 211 transmission services. The Commission's goal is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers.

EFFECTIVE DATE: This Final Rule will become effective on July 9. 1996.

FOR FURTHER INFORMATION CONTACT: David D. Withnell (Legal Information-Docket No. RM95-8-000). Office of the General Counsel. Federal Energy Regulatory Commission. 888 First Street NE., Washington, DC 20426, (202) 208-2063

Deborah B. Leahy (Legal Information--Docket No. RM94-7-001). Office of the General Counsel. Federal Energy Regulatory Commission. 888 First Street NE.. Washington, DC 20426. (202) 208-2039

Michael A. Coleman (Technical Information), Office of Electric Power Regulation, Federal Energy, Regulatory Commission, 888 First Street NE., Washington, DC 20426, (202) 208-1236.

SUPPLEMENTARY INFORMATION: In addition to publishing the full text of this document in the Federal Register, the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in the Public Reference Room at 888 First Street, NE., Washington, DC 20426.

The Commission Issuance Posting System (CIPS), an electronic bulletin board service, provides access to the texts of formal documents issued by the Commission. CIPS is available at no charge to the user and may be accessed using a personal computer with a modem by dialing 202-208-1397 if dialing locally, or 1-800-856-3920 if dialing long distance. CIPS is also available through the Fed World system (by modem or Internet). To access CIPS, set your communications software to 19200, 14400, 12000, 9600, 7200, 4800, 2400, or 1200 bps. full duplex, no parity, 8 data bits and 1 stop bit. The full text of this order will be available on CIPS indefinitely in ASCII and WordPerfect 5.1 format. The complete text on diskette in Wordperfect format may also be purchased from the

Commission's copy contractor, La Dorn Systems Corporation, also located in the Public Reference Room at 888 First Street NE., Washington, DC 20426.

Table of Contents

I. Introduction/Summary
II Public Reporting Burden
III. Background
IV. Discussion
A. Scope of the Rule
1. Introduction
2. Functional Unbundling
3. Market-based Rates
4. Merger Policy
5. Contract Reform
6. Flow-based Contracting and Pricing
B. Legal Authority
1. Bases for Legal Authority
2. Response to Commentators Opposing our Legal Authority
C. Comparability
1. Eligibility to Receive Non-discriminatory Open Access Transmission
2. Service that Must be Provided by Transmission Provider
3. Who Must Provide Non-discriminatory Open Access Transmission
4. Reservation of Transmission Capacity by Transmission Customers
5. Reservation of Transmission Capacity for Future Use by Utility
6. Capacity Reassignment
7. Information Provided to Transmission Customers
8. Consequences of Functional Unbundling
D. Ancillary Services

1. Definitions and Descriptions
2. Obligations of Transmission Providers and Transmission Customers with Respect to Ancillary Services
3. Unbundling and Bundling Ancillary Services
4. Reassignment of Ancillary Services
5. Pricing of Ancillary Services
6. Accounting for Ancillary Services
E. Real-Time Information Networks
F. Coordination Arrangements: Power Pools, Public Utility Holding Companies, Bilateral Coordination Arrangements, and Independent System Operators.
1.Tight Power Pools
2. Loose Pools
3. Public Utility Holding Companies
4. Bilateral Coordination Arrangements
G. Pro Forma Tariff
1. Tariff Provisions That Affect The Pricing Mechanism
2. Priority for Obtaining Service
3. Curtailment Provisions
4. Specific Tariff Provisions
H. Implementation
I. Federal and State Jurisdiction: Transmission/Local Distribution
J. Stranded Costs
1. Justification for Allowing Recovery of Stranded Costs.
2. Cajun Electric Power Cooperative, Inc. v. FERC
3. Responsibility for Wholesale Stranded Costs (Whether to Adopt Direct Assignment to Departing Customers)
4. Recovery of Stranded Costs Associated with New Wholesale Requirements Contracts
5. Recovery of Stranded Costs Associated with Existing Wholesale Requirements Contracts
6. Recovery of Stranded Costs Caused by Retail-Turned-Wholesale Customers

7. Recovery of Stranded Costs Caused by Retail Wheeling
8. Evidentiary Demonstration Necessary - Reasonable Expectation Standard
9. Calculation of Recoverable Stranded Costs
10. Stranded Costs in the Context of Voluntary Restructuring
11. Accounting Treatment for Stranded Costs
12. Definitions, Application, and Summary
K. Other
1. Information Reporting Requirements for Public Utilities
2. Small Utilities
3. Regional Transmission Groups
4. Pacific Northwest
5. Power Marketing Agencies
6. Tennessee Valley Authority
7. Hydroelectric Power
8. Residential Customers
V. Environmental Statement
VI. Regulatory Flexibility Act Certification
VII. Information Collection Statement
VIII. Effective Date

Regulatory Text

Appendices (These Appendices will not appear in the Code of Federal Regulations)
A. List of Section 211 Applications
B. List of Commenters in Docket Nos. RM95-8-000 and RM94-7-001
C. Allegations of Public Utilities Exercising Transmission Dominance
D. Pro Forma Open Access Transmission Tariff
E. List of Group 1 Public Utilities
F. List of Group 2 Public Utilities

G. Legal Analysis of Commission Jurisdiction Over the Rates, Terms and Conditions of Unbundled Retail Transmission In Interstate Commerce

H. U.S. NO/X/Emissions

Statement of Commissioner Hoecker

Statement of Commissioner Massey

I. Introduction/Summary

Today the Commission issues three final, interrelated rules designed to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers.[1] The legal and policy cornerstone of these rules is to remedy undue discrimination wires that control whether and to whom electricity can transported in interstate commerce. A second critical aspect of the rules is to address recovery of the transition costs of moving from a monopoly regulated regime to one in which all sellers can compete on a fair basis and in which electricity is more competitively priced.

[1] These rules are the rules on open access and stranded costs in the above dockets (*FERC Statutes and Regulations* ¶ 31,036) and an accompanying rule on Open Access Same-Time Information System and Standards of Conduct (OASIS Final Rule) (*FERC Statutes and Regulations* ¶ 31,037) being issued contemporaneously: The Commission also is issuing contemporaneously a notice of proposed rulemaking on capacity reservation open access transmission tariffs in Docket No. RM96-11-000. *FERC Statutes and Regulations* ¶ 32,517. These final rules and proposed rule are being published concurrently in the *Federal Register*.

In the year since the proposed rules were issued,[2] the pace of competitive changes in the electric utility industry has accelerated. By March of last year, 38 public utilities had filed wholesale open access transmission tariffs with the Commission. Today, prodded by such competitive changes and encouraged by our proposed rules, 106 of the approximately 166 public utilities that own, control, or operate[3] transmission facilities used in interstate commerce have filed some form of wholesale open access tariff. In addition, since the time the proposed rules were issued, numerous state regulatory commissions have adopted or are actively evaluating retail customer choice programs or other utility restructuring alternatives. These events have been spurred by continuing pressures in the marketplace for changes in the way electricity is bought, sold, and transported. Increasingly, customers are demanding the benefits of competition in the growing electricty commodity market.

[2] On March 29, 1995, the Commission issued two notices of proposed rulemaking concerning open access transmission and stranded cost recovery. Promoting Wholesale Competition Through Open-Access Non-Discriminatory Transmission Service by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, 60 FR 17662 (April 7, 1995). *FERC Statutes and Regulations* ¶ 32,514 (1995). On December 13, 1995, the Commission issued a notice of proposed rulemaking on information systems. Real-Time Information Networks and Standards of Conduct. Notice of Proposed Rulemaking, 60 FR 66182 (December 21, 1995), *FERC Statutes and Regulations* ¶ 32,516 (1995).

[3] The Commission's notice of proposed rulemaking in the above dockets proposed to apply the proposed requirements to public utilities that own and/or control facilities used for the transmission of electric energy in interstate commerce. "Own and/or control" is intended to include public utilities that "operate" facilities used for the transmission of electric energy in interstate commerce. However, we have modified the Final Rule regulatory text to remove any ambiguity.

The Commission estimates the potential quantitative benefits from the Final Rule will be approximately $3.8 to $5.4 billion per year of cost savings, in addition to the non-quantifiable benefits that include better use of existing assets and institutions, new market mechanisms, technical innovation, and less rate distortion. The continuing competitive changes in the industry and the prospect of these benefits to customers make it imperative that this Commission take the necessary steps within its jurisdiction to ensure that all wholesale buyers and sellers of electric energy can obtain non-discriminatory transmission access, that the transition to competition is orderly and fair, and that the integrity and reliability of our electricity infrastructure is maintained.

In this Rule, the Commission seeks to remedy both existing and future undue discrimination in the industry and realize the significant customer benefits that will come with open access. Indeed, it is our statutory obligation under sections 205 and 206 of the Federal Power Act (FPA) to remedy undue discrimination.

To do so, we must eliminate the remaining patchwork of closed and open jurisdictional transmission systems and ensure that all these systems, including those that already provide some form of open access, cannot use monopoly power over transmission to unduly discriminate against others. If we do not take this step now, the result will be benefits to some customers at the expense of others. We have learned from our experience in the natural gas area the importance of addressing competitive transition issues early and with as much certainty to market participants as possible.

Accordingly, in this proceeding and in the accompanying proceeding on OASIS the Commission, pursuant to its authorities under sections 205 and 206 of the FPA:

- Requires all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce:

- To file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service:

- To take transmission service (including ancillary services) for their own new wholesale sales and purchases of electric energy under the open access tariffs:

- To develop and maintain a same time information system that will give existing and potential transmission users the same access to transmission information that the public utility enjoys, and further requires public utilities to separate transmission from generation marketing functions and communications:

- Clarifies Federal/state jurisdiction over transmission in interstate commerce and local distribution and provides for deference to certain state recommendations; and

- Permits public utilities and transmitting utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and FPA section 211 transmission services.

Open Access

The Final Rule requires public utilities to file a single open access tariff that offers both network, load-based service and point-to-point, contract-based service. The Rule contains a pro forma tariff that reflects modifications to the NOPR's proposed terms and conditions and also permits variations for regional practices. All public utilities subject to the Rule, including those that already have tariffs on file, will be required to make section

206 compliance filings to meet the new pro forma tariff non-price minimum terms and conditions of non-discriminatory transmission. Utilities may propose their own rates in a section 205 compliance filing.

The Rule provides that public utilities may seek a waiver of some or all of the requirements of the Final Rule. In addition, non-public utilities may seek a waiver of the tariff reciprocity provisions.

The Final Rule does not generically abrogate existing requirements contracts, but will permit customers and public utilities to seek modification, or termination, of certain existing requirements contracts on a case-by-case basis. As to coordination arrangements and contracts, the Rule finds that these arrangements and contracts may need to be modified to remove unduly discriminatory transmission access and/or pricing provisions. Such arrangements and agreements include power pool agreements, public utility holding company agreements, and certain bilateral coordination agreements. The Rule provides guidance and timelines for modifying unduly discriminatory coordination arrangements and contracts, and specifies when the members of such arrangements must begin to conduct trade with each other using the same open access tariff offered to others. The Rule also provides guidance regarding the formation of independent system operators (ISOs).

The Rule does not require any form of corporate restructuring, but will accommodate voluntary restructuring that is consistent with the Rule's open access and comparability policies.

As discussed in the NOPR, not all owners or controllers of interstate transmission facilities are subject to the Commission's jurisdiction under sections 205 and 206 of the FPA and therefore are not subject to this Rule's open access requirements.

Therefore, the Final Rule retains the proposed reciprocity provision in the pro forma tariff. Without such a provision, non-open access utilities could take advantage of the competitive opportunities of open access, while at the same time offering inferior access, or no access at all, over their own facilities. Thus, open access utilities would be unfairly burdened. We note that some non-jurisdictional utilities have expressed an interest in a mechanism for obtaining a Commission determination that their transmission tariffs satisfy the reciprocity provisions in the pro forma tariffs, and we provide such a mechanism in the Rule.

The Final Rule does not generically provide for market-based generation rates. Although the Rule codifies the Commission's prior decision that there is no generation dominance in new generating capacity, intervenors in cases may raise generation dominance issues related to new capacity. In addition, to obtain market-based rates for existing generation, we will continue to require public utilities to show, on a case-by-case basis, that there is no generation dominance in existing capacity. Further, in all market-based cases, we will continue to look at whether an applicant and its affiliates could erect other barriers to entry and whether there may be problems due to affiliate abuse or reciprocal dealing.

Finally, contemporaneously with this Rule the Commission issues an NOPR on capacity reservations tariffs as an alternative, and perhaps superior, means of remedying undue discrimination.

Transmission/Local Distribution

The Rule clarifies the Commission's interpretation of the Federal /state jurisdictional boundaries over transmission and local distribution. While we reaffirm our conclusion that this Commission has exclusive jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate

commerce by public utilities, we nevertheless recognize the very legitimate concerns of state regulatory authorities as they contemplate direct retail access or other state restructuring programs. Accordingly, we specify circumstances under which we will give deference to state recommendations. Although jurisdictional boundaries may shift as a result of restructuring programs in wholesale and retail markets, we do not believe this will change fundamental state regulatory authorities, including authority to regulate the vast majority of generation asset costs, the siting of generation and transmission facilities, and decisions regarding retail service territories. We intend to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies.

Stranded Costs

With regard to stranded costs, the Final Rule adopts the Commission's supplemental proposal. It will permit utilities to seek extra-contractual recovery of stranded costs associated with a limited set of existing (executed on or be fore July 11, 1994) wholesale requirements contracts and provides that the Commission will be the primary forum for utilities to seek recovery of stranded costs associated with retail-turned-wholesale transmission customers. It also will allow utilities to seek recovery of stranded costs caused by retail wheeiing only in circumstances in which the state regulatory authority does not have authority to address retail stranded costs at the time the retail wheeling is required. The Rule retains the revenues lost approach for calculating stranded costs and provides a formula for calculating such costs.

Environmental Issues

The Commission has prepared a Final Environmental Impact Statement (FEIS) evaluating the possible environmental

consequences of changes in the bulk power marketplace expected to occur as a result of the open access requirements of this Final Rule. The FEIS focuses, as do most commenters, on possible increases in emissions of nitrogen oxides (NO/X/) from certain fossil-fuel fired generators, which could affect air quality in the producing region and in areas to which these emissions may be carried.

In response to comments on the Draft EIS, the Commission performed numerous additional studies. The FEIS finds that the relative future competitiveness of coal and natural gas generation is the key variable affecting the impact of the Final Rule. If competitive conditions favor natural gas, the Rule is likely to lead to environmental benefits. Both EPA and the Commission staff believe this projected scenario is the more likely one. If competitive conditions favor coal, the Rule may lead to small negative environmental impacts. However, even using the most extreme, unlikely assumptions about the future of the industry, the negative consequences are not likely to occur until after the turn of the century. Because the impacts will remain modest at least until 2010, there is no need for an interim mitigation program. In addition, even if the data showed more significant negative consequences requiring mitigation, the Commission does not have the statutory authority under the Federal Power Act or the expertise to address this possible far-term problem. The Commission believes, however, that there is time for federal and state air quality authorities to address any potential adverse impact as part of a comprehensive NO_x regulatory program under the Clean Air Act.

Despite our conclusions regarding the lack of environmental impacts expected to result from the Rule, the Commission has expected to result from the Rule, the Commission has examined a wide variety of proposals for mitigating possible adverse effects. We share the view of most commenters that the preferred approach for mitigating increased NO/X/ emissions

generally is a NO/X/ cap and trading regulatory program comparable to that developed by Congress to address sulfur dioxide emissions in the Clean Air Act Amendments of 1990.[5] The Commission has examined various means of establishing such a program, including use of existing federal authorities under the Clean Air Act, cooperative efforts by state and federal air quality regulators, and development of a new emissions regulatory program administered by the Commission under the Federal Power Act. The Commission has concluded that a NO/X/ regulatory program could best be developed and administered under the Clean Air Act, in cooperation with interested states, and offers to lend Commission support to that effort should it become necessary.

Conclusion

The Commission believes that the Final Rule will remedy undue discrimination in transmission services in interstate commerce and provide an orderly and fair transition to competitive bulk power markets.

II. Public Reporting Burden

The Open Access Final Rule and the Stranded Cost Final Rule specify filing requirements to be followed by public utilities that own, control or operate transmission facilities in interstate commerce in making non-discriminatory open access tariff filings and filings to recover legitimate, prudent and verifiable stranded costs. The information collection requirements of the final rules are attributable to FERC-516 "Electric Rate Filings." The current total annual reporting burden for FERC-516 is 828,300 hours.

---

[5] 42 U.S.C.A. § 7651b-e

A. *Docket No. RM95-8-000 (Open Access Final Rule)*

The Open Access Final Rule requires public utilities filing non-discriminatory open access tariffs to provide certain information to the Commission. The Commission estimated that the public reporting burden for the information collection would average 300 hours per response. This estimate included time for reviewing the requirements of the Commission's regulations, searching existing data sources, gathering and maintaining the necessary data, completing and reviewing the collection of information and filing the revised information. No cormments on the burden estimate were received. Because the Final Rule adopts essentially the same information requirements that are contained in the proposed rule, we believe that the average filing burden is same for the Final Rule.

In the proposed rule, the Commission noted that there are approximately 328 public utilities, including marketers and wholesale generation entities. We initially estimated that 137 public utilities own, control or operate facilities used for the transmission of electric energy in interstate commerce, and would be subject to the filing requirements of the proposed rule. Upon further review, the Commission believes that approximately 166 public utilities will respond to the information collection. Accordingly, the public reporting burden is estimated to be 49.800 hours.

B. *Docket No. RM94-7-001 (Stranded Cost Final Rule)*

In the supplemental notice of proposed rulemaking, the Commission estimated that the information requirements of the proposed rule would not differ substantially from those contained in the initial proposed rule. In that notice. the Commission estimated that the public reporting burden for the information requirements contained in the proposed rule would be 50 hours per response with 10 responses annually. No

comments on this filing burden were received. The information requirements adopted in the Stranded Cost Final Rule are not substantially different from those in the proposed rule. Therefore, the Commission concludes that there will be no additional public filing burden associated with the Stranded Cost Final Rule.

III. Background

In the NOPR, set out a detailed statement of the events leading up to this rulemaking. We repeat that background here, updated to reflect what has happened since March 1995, and discuss why it is necessary to undertake regulatory reform in the electric industry at this time. We do so to provide the necessary

* * * * *

specifically allow utilities either to follow the terms of the provision or to use alternatives that are reasonable, generally accepted in the region, and consistently adhered to by the transmission provider (e.g.. time deadlines for scheduling changes, time deadlines for determining available capacity). In addition, other tariff provisions require utilities to follow Good Utility Practice, The definition of "Good Utility Practice," contained in Section 1.14 of the Final Rule pro forma tariff, states, that it "is not intended to be limited to the optimum practice. method, or act to the exclusion of all others, but rather to be acceptable practices, methods or acts generally accepted in the region." Thus, where public utilities are permitted to follow regional practices. and elect to do so within 60 -days of the date of publication of the Final Rule in the Federal Register, they should identify the regional practices in their compliance tariff filings.

4. Future Filings

We recognize that there may be circumstances in which a public utility believes that the Final Rule pro forma tariff does not provide sufficient flexibility or that the utility can propose superior nonrate terms and conditions. Thus, once the compliance tariff and conforming rates go into effect, which will be 60 days after publication of this Rule in the Federal Register, a public utility (either Group 1 or Group 2) may file pursuant to section 205 a tariff with terms and conditions that differ from those set forth in this Rule, provided that it: (1) Serves a copy of its filing on all wholesale customers for whom it has provided transmission service since March 29, 1995 (the date of the Open Access NOPR) and on the state agencies that regulate public utilities in the states where those customers are located; (2) identifies all deviations from its compliance tariff in its letter of transmittal; (3) provides, to the extent practical, a redlined version of the tariff; and (4) demonstrates that such terms and conditions are consistent with, or superior to, those in the compliance tariff. However, it may not seek to litigate fundamental terms and conditions set forth in the Final Rule.[514] In addition, the public utility may file whatever rates it believes are appropriate, consistent with the Transmission Pricing Policy Statement.

---

[514] As we stated in our "Further Guidance Order," American Electric Power Service Corp., 71 FERC ¶61,393, 62,539-40, order on rehearing, 72 FERC ¶ 61,287, order on rehearing, 74 FERC ¶ 61,013 (1995), all tariffs need not be "cookie-cutter" copies of the Final Rule tariff. Thus, under our new procedure, ultimately a tariff may go beyond the minimum elements in the Final Rule pro forma tariff or may account for regional, local, or system-specific factors. The tariffs that go into effect 60 days after publication of this Rule in the Federal Register will be identical to the Final Rule pro forma tariff; however, public utilities then will be free to file under section 205 to revise the tariffs, and customers will be free to pursue changes under section 206.

5. Waiver

Finally, as noted above, several commenters propose that public utilities that own few transmission facilities be granted waiver, or that application of the Rule to such utilities be deferred until 60 days after they receive a section 211 request. As discussed more fully in Section IV.K.2, we find that it is reasonable to permit certain public utilities for good cause shown to file, within 60 days after this Rule is published in the Federal Register, requests for waiver from some or all of the requirements of this Rule. The filing of a request in good faith for a waiver from the requirement to file an open access tariff will eliminate the requirement that such public utility make a compliance filing unless thereafter ordered by the Commission to do so. It will not, however, exempt such public utility from providing upon request, transmission services consistent with the requirements of the Final Rule.

I. Federal and State Jurisdiction: Transmission/Local Distribution. In the original Stranded Cost NOPR, the Commission clarified that it has exclusive jurisdiction, over unbundled retail transmission in interstate commerce by public utilities: it found that the Commission has exclusive jurisdiction over the rates, terms. and conditions of unbundled retail transmission in interstate commerce by public utilities, up to the point of local distribution. In the Open Access NOPR, the Commission reaffirmed this jurisdictional determination[515] and

[515] That determination included the situation in which a former bundled retail customer may need unbundled wheeling services from its previous public utility generation supplier, as well as unbundled wheeling from one or more intervening public utilities, in order to reach a distant generation supplier. In that scenario, the Commission would have jurisdiction over all of the transmission facilities used for the unbundled wheeling provided by the intervening public utilities. The NOPR also noted that the Commission would not have jurisdiction over the rates for the sale of generation by the distant supplier because the transaction would be a retail sale. *FERC*

also addressed the distinction between transmission and local distribution. The Commission stated three reasons for expressing its views on the distinction between Commission-jurisdictional transmission in interstate commerce and state jurisdictional local distribution, in the context of unbundled retail wheeling by public utilities.[516] First, facilities that can be used for wholesale transmission in inter-state commerce by a public utility would be subject to the Commission's open access requirements. Second, states have authority to address retail stranded costs and stranded benefits through their jurisdiction over facilities used in local distribution. Third, as the structure of the industry continues to change dramatically, utilities need to know which regulator has jurisdiction over which facilities and services in order to meet state and federal filing requirements. Accordingly, the NOPR set forth our jurisdictional analysis and several technical factors, for determining what constitutes "facilities used in local distribution."

For unbundled wholesale wheeling, the NOPR proposed to apply a functional test. i.e., whether the entity to whom the power is delivered is a lawful reseller. For unbundled retail wheeling, the NOPR proposed to apply a combination functional technical test that would take into account technical characteristics of the facilities used for the wheeling. The Commission proposed seven indicators of local distribution to be evaluated on a case-by-case basis:

Statutes and Regulations ¶32,514 at p. 33,144.

[516] The term "wheeling" is intended to cover any delivery of electric energy from a supplier to a purchaser, i.e., transmission, distribution, and/or local distribution. The Commission also has jurisdiction to order wholesale transmission services in either interstate or intrastate commerce by transmitting utilities that are not also public utilities. *See Tex-La Electric Cooperative of Texas, Inc.*, 67 FERC ¶61,019 (1994) reh'g pending.

(1) Local distribution facilities are normally in close proximity to retail customers.

(2) Local distribution facilities are primarily radial in character.

(3) Power flows into local distribution systems; it rarely, if ever, flows out.

(4) When power enters a local distribution system, it is not reconsigned or transported on to some other market.

(5) Power entering a local distribution system is consumed in a comparatively restricted geographical area.

(6) Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

(7) Local distribution systems will be of reduced voltage. [517]

The NOPR concluded that the application of these tests will enable states to address stranded costs by imposing an exit fee on departing retail customers, or including an adder in the retail customers' local distribution rates.[518]

In the NOPR. the Commission also addressed buy-sell transactions in which an end user arranges for the purchase of generation from a third-party supplier and a public utility transmits that energy in interstate commerce and resells it as part of a "nominal" bundled retail sale to the end user. We explained that the retail sale is actually the functional equivalent of two

[517] *FERC Statutes and Regulations* ¶ 32,514 at p. 33,145.

[518] Id. at p. 33,144-45.

unbundled sales (one transmission and the other the sale of power) and that we have exclusive jurisdiction over the voluntary sale by public utilities of unbundled transmission at retail in interstate commerce.[519]

Several commenters support the Commission's proposed Jurisdictional demarcation.[520] San Diego G&E states that the Commission correctly proposed to look at both functional factors (such as whether the service is retail or wholesale) and technical factors (such as voltage). PG&E states that the NOPR's functional/technical test is preferable to a bright line voltage test.

Consumers Power states that the Commission has exclusive jurisdiction over all wheeling on an interconnected interstate transmission grid. It suggests that the Commission and the states act through a joint board or hearing to resolve jurisdictional differences and develop a bright line test.

PSE&G and PG&E: express concern that if retail wheeling is implemented, there may be loopholes that would enable customers to evade state jurisdiction and thus avoid paying stranded costs. For example, PSE&G is concerned that a retail customer may request transmission service only and a state commission will be unable to attach a retail stranded cost surcharge to that customer. PG&E proposes, adding another indicator to the functional/technical test— a final tap to a retail customer—to ensure that "high-voltage" retail customers do not evade the state's reach. Moreover, to ensure that retail customers cannot escape state jurisdiction, PG&E recommends that the Commission state, as a matter of policy, that "all retail

[519] As discussed *infra*, there also would be a component of local distribution in such a transaction that would be subject to state jurisdiction.

[520] *E.g.* PG&E, Wisconsin Coalition, Com Ed.

customers taking retail transmission service from their host utility by definition take service over local distribution facilities."

CINergy agrees with the Commission that a distinction between transmission and local distribution is important, but emphasizes the practical need for clarity on a timely basis. To achieve certainty, CINergy proposes that the Commission allow public utilities to file, under section 205, classifications of their facilities as transmission or local distribution. CCEM endorses CINergy's proposal. Although NARUC disagrees that the Commission has jurisdiction over unbundled retail transmission, if the Commission reaffirms the NOPR regarding its jurisdiction, then NARUC supports CINergy's proposal.

PSE&G strongly supports the Commission's proposed case-by-case methodology for determining whether facilities should be classified as transmission or local distribution. SoCal Edison argues that since a utility may have difficulty determining which of its facilities are transmission and which are local distribution, utilities and states should be able to ask the Commission to classify a particular facility. Portland and Orange & Rockland suggest that the Commission provide a forum to resolve disputes over the correct classification of particular facilities.

Ohio Edison states that the Commission should assume jurisdiction over unbundled retail transmission, but only where a state has required this unbundling. It also believes that the Commission should assert jurisdiction over the ancillary services necessary to provide this jurisdictional service.

NYSEG argues that the Commission lacks jurisdiction over the transmission component of bundled retail service. On the other hand. NYSEG argues that the statute, legislative history, and case law reveal that the Commission has jurisdiction over

unbundled retail wheeling from source to load, since it is transmission in interstate commerce. NYSEG argues that the "local distribution" exception to the Commission's jurisdiction applies only to bundled sales of power at retail.

Several state commissions assert that states have rate authority over all facilities used to provide retail service.[521] IL Com argues that states have rate authority over all facilities used to provide retail service, regardless of whether the NOPR would classify these facilities as transmission or local distribution.

MI Com, citing Connecticut Light & Power Company v. Federal Power Commission, 324 U.S. 5 15 (1945) (CL&P), and Arkansas Electric Cooperative v. Arkansas Public Service Commission, 461 U.S. 375, 393-94 (1983), contends that states have plenary jurisdiction over all aspects of retail service, including retail access and unbundled retail transmission service. It asserts that the Commission's effort to expand federal jurisdiction into transmission in connection with retail sales is without statutory justification.

Legal Environmental Assistance argues that the NOPR creates confusion about, and may intrude onto, state jurisdiction. NYMEX argues that when a state orders retail wheeling, the state should have jurisdiction over that transmission-only service.

Oklahoma G&E, citing CL&P and United States v. California Public Utilities Commission, 345 U.S. 295, 316 (1953), asserts that the Commission failed to explain that the term "transmission in interstate commerce" could have different meanings depending on the factual context in which the term is applied. It argues that "transmission in interstate commerce"

---

[521] *E.g.* NM Com, NC Com, AZ Com.

means the movement, in bulk, of electric energy flowing in interstate commerce, as opposed to the movement of electric energy that has been subdivided for delivery to consumers.

Oklahoma G&E further argues that "[t]he distinction between interconnected operation and radial operation corresponds precisely to this distinction between activities that have potential interstate effects and those that might have interstate effects but are a matter of primarily local concern."[522] Oklahoma G&E also disagrees that the transportation of electric energy sold at wholesale necessarily constitutes transmission in interstate commerce. It argues that the Commission has misapplied case precedent and, by focusing on the level of the associated power sale, the Commission has misunderstood what constitutes a functional distinction between transmission in interstate commerce and local distribution.

NY Com asserts that the grant of jurisdiction to the Commission over wholesale power transactions in interstate commerce under section 201 of the FPA does not reduce the states' authority over local distribution (citing CL&P and Federal Power Commission v. Florida Power & Light Company, 404 U.S. 453, 467 (1972)). NY Cam argues that the NOPR's assertion of exclusive jurisdiction over all facilities used to deliver electricity for resale, even those traditionally regarded as local distribution, violates Congress' assignment of local electric distribution to the states. It takes issue with the Commission's list of factors and says that states and the Commission should agree on a definition that preserves the traditional classification of local distribution facilities. According to NY Com, such definition should focus on the functional characteristics of local electric systems - i.e., electricity flows into a comparatively

[522] Oklahoma G&E Initial Comments at p. 16.

restricted geographic area and does not flow back out of that area, and the power is consumed in that area.

NY IOUs argue that the Commission has jurisdiction over unbundled, but not bundled retail wheeling. It says that other factors, including the indicators listed in the NOPR, are irrelevant, and that even long-distance interstate transmission is under state jurisdiction as long as it is bundled with a retail sale. According to NY IOUs, this is the plain meaning of the FPA; resort to legislative history is unnecessary. NY IOUs bases this view on section 201(a), which says that federal regulation extends only to matters not subject to state regulation. NY IOUs says that the only matters subject to state regulation were bundled retail sales, and that since transmission was part of the bundle, Congress intended transmission to stay under state authority as long as it is part of that bundle. It also cites section 201(b), which sets forth exceptions from Commission jurisdiction, and section 201(c), which defines "transmission in interstate commerce" and thus also controls the definition of transmission in intrastate commerce. Finally, NY IOUs argues that the legislative history supports its view, as does the case law.

Central Louisiana believes that the costs of requiring a transmission provider to take unbundled transmission service for both wholesale and retail purposes would far exceed any benefits. In this regard, Central Louisiana says that states clearly have jurisdiction over bundled retail transmission charges and that the proposed approach could not be implemented without states giving up jurisdiction or the passage of new federal legislation.

MN DPS disagrees on legal and policy grounds with the Commission's assertion of jurisdiction over unbundled retail

transmission services.[523] It maintains that the Commission's arguments do not negate the language of the FPA specifying that regulation of retail sales of electric energy is reserved to the states. MN DPS argues that the Commission's arguments in support of its position are not on point because the issue is state authority to set rates for retail sales, not inter-state commerce. Further, it declares that jurisdiction over a service does not change simply because it is priced differently.

Several commenters argue that unbundled pricing should not expand the Commission's jurisdiction. [524] NARUC argues that the NOPR did not explain why the Commission's authority attaches only to unbundled retail transmission service, why unbundling is jurisdictionally significant, and how transmission of electricity to end users differs from unbundled interstate transmission of natural gas by local distribution companies, which is subject to state regulation. Thus, NARUC, urges the Commission not to claim jurisdiction over unbundled retail transmission services.

NARUC also argues that the Commission's test for distinguishing between transmission and local distribution is not a bright line as discussed in Federal Power Commission v. Southern California Edison Company, 376 U.S. 205 (1964) (Colton). NARUC concludes that when a state determines to enable a retail customer to purchase power from a third-party provider, that state retains the authority to regulate the delivery service provided by the utility.

IL Com asserts that the test should be whether the utility function over which the Commission seeks to exercise

[523] See also OH Com.

[524] *E.g.*, DOD, NM Com, KY Com. ABATE.

jurisdiction is one which falls within the Attleboro gap.[525] It argues that the Commission has no legal authority to prescribe conditions under which a public utility may provide transmission service within its own service territory to its own retail customers. IL Com concedes that the court cases cited by the Commission can be interpreted to support widely disparate legal and policy positions, but argues that those cases resolved questions of Commission jurisdiction in circumstances where wholesale sales of electric power were being examined and not circumstances where retail sales are being considered. It contends that the question of whether the Commission should exercise jurisdiction over all transmission in retail wheeling has never been addressed before and requires a careful examination of the underlying purposes of Congress in enacting the FPA. IL Com explains that transmission by an Illinois utility of power to a retail consumer within its own service territory is not subject to Commission jurisdiction because that transmission was never within the Attleboro gap and has always been regulated by states.

OK Com recommends that the Commission apply to the electric industry the same policy that it has adopted concerning its regulation of the gas industry and leave unbundled retail service regulation to state authorities.

WI Com argues that if a utility offers unbundled retail access, jurisdiction over transmission services should continue to be based upon the historical demarcation between wholesale and retail transactions. KY Com argues that Congress did not intend, by authorizing wholesale wheeling in the Energy Policy Act, to change the longstanding division of jurisdiction between the Commission and the states. It claims that the NOPR ignores the

[525] *See Public Utilities Commission v. Attleboro Steam & Electric Company*, 273 U.S. 83 (1927).

limitation in the FPA that the Commission has no jurisdiction over retail sales service. NV Com cites several cases noting the states' historical authority to regulate retail rates.

IA Com proposes a definition of local distribution and transmission that would preserve the jurisdictional status quo and does not put a state commission in the position of losing authority over certain elements of a retail transaction should it allow retail wheeling. IA Com's proposed definition is as follows:

Distribution - Service provided by a utility directly connected to an ultimate consumer of electricity is a distribution service with respect to electric energy delivered to that consumer.

Transmission - Service provided by a utility with respect to electric energy to be delivered to an ultimate consumer through another utility is a transmission service.[526]

Montana Power states that a reasonable way to give effect to the "local distribution" exemption is to define "local distribution" as a bundled retail sale, even if interstate facilities are used.

Several commenters criticized the NOPR's functional/physical indicators. PA Com disagrees with the Commission's discussion of the FPA's legislative history and asserts that the FPA does not address the issue of what constitutes local distribution. PA Com contends that the issue was resolved by the Supreme Court in CL&P in a manner contrary to the Commission's technical-functional test and that the NOPR minimized CL&P. NM Com asserts that the proposed engineering and functional elements for determining the status of local distribution facilities

[526] IA Com Initial Comments at p. 4.

fail to account for the governmental or legalistic test requirement of the FPA as identified in CL&P.

KY Com concludes that a physical definition of distribution facilities. based on objective criteria, is consistent with the FPA and is necessary to provide a clean line of demarcation.

CO Com argues that Congress used a transactional test rather than a functional test and that Congress intended all retail transactions to be under state jurisdiction. According to CO Com, there is concurrent jurisdiction over unbundled transmission in interstate commerce to an end-user. Moreover, CO Com asserts that unbundled intrastate transmission to a wholesale purchaser is under state jurisdiction (citing section 201(b)(l)). Finally, CO Com argues that the state has authority over unbundled transmission in intrastate commerce to an end-user when the transmission-providing utility, end-user, and generator are all within the same state.

Other commenters prefer a functional test. Natural Resources Defense, DOE, and Sustainable Energy Policy generally agree that a line needs to be drawn between transmission and local distribution but believe that the Commission's test is unnecessarily cumbersome or may lead to legal uncertainty, at least within the context of stranded benefits. Instead, Natural Resources Defense proposes the following functional test, which is based on end-use service:

The Federal Power Act does not affect state regulators' jurisdiction to apply distribution charges - either volume-based or fixed - to electricity that is used by any utility customer to provide end-use services (as distinguished from electricity that

is purchased for resale to end-use customers).[527] Sustainable Energy Policy endorses Natural Resources Defense's position. DOE suggests that a functional definition of local distribution (i.e., electricity provided for end-use service) may be the best way to avoid legal uncertainty.

EPA argues that the Commission's proposed physical definition may encourage gaming to avoid stranded costs and costs associated with public policy goals such as energy efficiency, renewable energy development costs and R&D funding, and a physical definition assumes that power flows into, and not out of, distribution systems, which would not allow for distributed generation (e.g.. fuel cells). Thus. EPA urges the Commission to adopt a functional definition that "local distribution occurs whenever electricity is provided by a utility for end-use service." Alternatively. EPA suggests that the Commission add a provision to its approach that "the provision of electricity for end-use service generally involves local distribution." Sustainable Energy Policy suggests a nonbypassable charge levied on all users of the distribution system. It endorses the policy formulation set forth by Natural Resources Defense in its initial comments. Reynolds wants to ensure that there is always at least concurrent state jurisdiction over lines used to serve enduse customers, since only states can order retail wheeling.

Detroit Edison argues that state/federal jurisdictional issues should be resolved by focusing on the use of the facilities. It says that facilities that are used to distribute a utility's own power to its own local customers should be subject to state regulation, while the use of facilities for wholesale power transactions or wholesale or retail transmission in interstate commerce should be under federal regulation.

---

[527] Natural Resources Defense Initial Comments at p.3.

Mountain State Petroleum Assoc. argues that the Commission should use a functional test based on state boundaries: if a line is in more than one state. there is Commission jurisdiction; if a line is entirely within one state. there is state jurisdiction.

MD Com states that it believes that the Commission's proposed indicators for determining where to draw the line are adequate, but adds that it does not concede the Commission's assertion of jurisdiction over unbundled retail transmission.

Some commenters suggest that implementation of the NOPR's tests could have adverse consequences. NH Com objects to the NOPR's specific tests; for example, if the Commission asserts jurisdiction over facilities because they are not radial. New Hampshire's policy of encouraging looping rather than radial lines would have the ironic effect of destroying state jurisdiction. NJ BPU states that there may be situations when the NOPR factors would not produce the proper result. It requests that the final rule recognize the need for case-by-case flexibility in determining where federal jurisdiction ends, so that the Commission and the states can work cooperatively.

NRRI argues that the NOPR's test could make siting of new transmission lines more difficult because states have in the past required native load customers to pay that part of the transmission-related revenue requirement that is not covered by unbundled transmission service. NRRI contends that, if the Commission asserts jurisdiction over all unbundled transmission service and if there is a firm point-to-point service capacity right that has value and is reassignable, then state commissions might eliminate portions of the transmission systems subject to capacity rights from rate base. NRRI is also concerned that the NOPR's transmission/local distribution test could create a price squeeze between bundled and unbundled retail transmission rates.

IN Com argues that the NOPR's view of jurisdiction would discourage retail wheeling. It says that states will be reluctant to order wheeling if the result is that they lose jurisdiction over the previously rolled-in transmission aspect of the service. It suggests that the Commission use negotiated rulemaking to address jurisdictional issues.

Several commenters suggest alternative approaches to jurisdictional line-drawing. NV Com suggests that the Commission consider federal and state jurisdiction over transmission by using "network" and "non-network" concepts:

The "network" concept for regulation recognizes that there is an interstate network of electric facilities used to link generation with loads. The operation of that network is indifferent to whether the electrical flows are retail or wholesale flows. Conceptually, events on the network could fall under federal jurisdiction. Where facilities provide essential service for the delivery of power, but do not substantially affect the electrical flows on the network, the facilities fall outside the network and would remain within the traditional domain of the state commission. As a consequence the delineation of federal and state jurisdiction evolves from the recognition of the events and where they occur as opposed to a rigid consideration of the physical properties of the facilities involved.[528]

NV Com further explains that the determination of what is a network event would require a case-by-case examination.

OH Com asserts that Congress intends there to be a bright line between state and federal jurisdiction and that the Commission has failed to provide such a bright line. OH Com proposes the use of retail marketing areas to provide the bright line—the

[528] NV Com Reply Comments at p. 3

jurisdictional line would be at the point at which power enters the retail marketing area of the entity delivering the power to the retail customer. OH Corn cites section 212(g) Of the FPA, as amended by the Energy Policy Act, which provides that the Commission cannot issue any order under the FPA inconsistant with state law governing retail marketing areas.

Under OH Com's proposal, the Commission would have jurisdiction over the wheeling-out and wheeling-through components of retail wheeling and the state would have jurisdiction over the wheeling-in component due to its local nature. OH Com concludes that the Commission's approach "fails to-meet the legal standard FERC must consider, and is inconsistent with the 'savings clause' and legitimacy of 'retail marketing areas' as discussed in the amended FPA."[529] OH Com also explains that the Commission's approach "is wreaking havoc on the state's ability to develop an interruptible buy-through arrangement to provide an increased competitive option for its retail customers."[530] OH Com further encourages the use of mutual deference to promote Congress intent in mandating a system of federal/ state cooperation. In support, OH

[529] Sections 212(g) and 212(h) of the FPA.

[530] We note that since OH Com filed its comments, it approved an interruptible buy-through plan, *See Interruptible Electric Service Guidelines*, Case No. 95-866-EL-UNC,—PUR 4th—(Ohio PUC Feb. 15, 1996). *See also Central Illinois Light Company*, Docket No. ER96-1075-000 (1996) (accepting amendment to open access transmission tariffs that expands service eligibility to accommodate participation in experimental retail wheeling pilot program approved by the Illinois Commerce Commission): *Illinois Power Company*, Docket No. ER96-1285-000, 75 FERC (1996): *cf. Illinois Power Company*,—PUR4th—, NO. 95-0494 (Illinois Commerce Commission Mar. 13, 1996) (offering retail direct access service providing transmission and ancillary services using the rates, terms, and conditions of Illinois Power's open access tariff on file with the Commission); recently introduced legislation in Rhode Island, H.B. 8124, the Utility Restructuring Act of 1996.

Com cites federal and state enforcement of telecommunications laws. NRRI also suggests that the jurisdictional line be drawn at the retail marketing area.

DC Com argues that the NOPR test is too difficult to administer and will create problems in determining the rate base at the state level. It suggests that the Commission should have jurisdiction over transmission from the source to the boundary of the "home" utility that delivers the power to the customer, with state jurisdiction over all aspects of the transmission service within that utility's franchise territory. AZ Com also expresses doubts that the NOPR's test is workable.

Several commenters propose that the Commission and state authorities address the jurisdictional issue jointly. SBA characterizes the Commission's proposed demarcation line as "laudable but misguided."[531] SBA recommends that a federal/state board be established to resolve the transmission/local distribution dilemma, similar to what Congress did for allocating costs between interstate and intrastate communications. SBA explains that the problem in the communications industry was the impossibility of allocating a portion of a single copper wire to interstate or intrastate service.

AZ Com notes that even if the Commission is correct, the FPA clearly does not preempt a state from concluding that retail transmission or other direct access programs should be implemented in that state. AZ Com suggests that there may be concurrent jurisdiction and that mutually agreed-upon principles should be implemented to determine which jurisdiction should be given deference.

---

[531] SBA Initial Comments at p. 36.

MD Com states that in determining tht status of particular facilities, the Commission should give substantial weight to determinations made by states. ABATE states that the Commission could initially defer to states with respect to the determination of rates, terms, and conditions, while maintaining the right to review and overturn the state determination.

If the Commission maintains its position concerning jurisdiction. NARUC argues that the Commission should not implement its multi-factor test, but should enter into discussions with state commissions to develop workable alternatives. NH Com argues that pricing the retail part of a transaction, even if it involves use of the transmission system, should be subject only to state jurisdiction. NH Com wants to create a mechanism by which state and federal regulators combine their efforts in cooperative regulation; it suggests several alternatives such as state/federal agreements for shared jurisdiction.

KY Com and NRRI object to the statement in the NOPR that retail buy-through service is really transmission service (subject to the Commission's jurisdiction) plus a sale of generation at retail (subject to state jurisdiction). From a policy standpoint, KY Com argues that the Commission's approach creates a powerful disincentive for a state to embark on changes that otherwise might foster a more competitive environment. NRRI argues that the Commission's approach may violate sections 212(g) and 212(h).

IL Com is concerned that industrial customers who get direct access may attempt to evade state, jurisdiction, and thus avoid retail stranded cost charges, by bypassing facilities, such as radial lines. It contends that retail wheeling rate surcharges would be a more effective means of recovering retail stranded costs if states were allowed to apply them to unbundled transmission and local distribution rates, not just the local distribution component of such rates.

NC Com asserts that "(a) significant cottage industry may well arise solely to convert retail customers. into wholesale customers, thereby subverting the intent of Congress as expressly set forth in EPACT."[532] If the Commission does not adopt NARUC's proposal, NARUC asserts that the Commission's functional test should not permit an end user to bypass the distribution service provided by the utility. It urges the Commission to assure that there will be some facility involved in the transaction that will be defined as providing a local distribution service.

NARUC also requests that the following sentence be added to proposed 18 CFR 35.27:

Nothing in this part limits the authority of a State commission in accordance with State law (1) to allow or disallow the inclusion of the costs of electric energy purchased at wholesale in retail rates subject to such State commission's jurisdiction, (2) to establish competitive procedures for the acquisition of such electric energy, or (3) to establish nondiscriminatory fees for the delivery of such electric energy to retail consumers for purposes established in accordance with State law.([533])

Duke is concerned about the potential for regulatory gaps, which could lead to costs not being recovered from either federal or state jurisdiction. Duke is also concerned that where facilities are used for both wholesale and retail transactions, costs might not be recovered if federal and state regulators use different methods of cost allocation.

---

[532] NC Com Initial Comments at p.7.

[533] NARUC Reply Comments at p. 15-16.

In response to the NOPR's proposal for functional unbundling,[534] CA Com agrees that it is important to draw a distinction between transmission and local distribution and that a bright line is not possible, but suggests that corporate or functional unbundling might provide a means to establish a workable bright line without relying on the more qualitative approach proposed in the NOPR. Arizona argues that rather than unbundling transmission for retail purposes, each utility should establish a distribution function that would obtain transmission on behalf of retail customers, taking service under the utility's tariff. Arizona states that this would simplify the allocation of transmission costs, since all transmission costs would be under the Commission's jurisdiction. Arizona argues that the Commission should permit the utility to recover the distribution rate approved by the state. According to Arizona, this would create a bright line between state and federal jurisdiction.

TX Com argues that the proposed text would not be applicable to intrastate utilities in Texas because they do not operate in interstate commerce. Thus, it asserts that it should continue to regulate Electric Reliability Council of Texas (ERCOT) transmission and distribution service and deal with stranded cost issues that arise in connection with any retail wheeling initiatives.

Several commenters object to the Commission's proposal to assert jurisdiction over transactions that are buy-sell transactions in name only.[535] AEP argues that the Commission should avoid an unnecessary conflict over state/federal jurisdiction, that may be caused by the NOPR's statement that buy-sell transactions are in fact transmission subject to Commission Jurisdiction. It

---

[534] *FERC Statutes and Regulations* ¶32,514 at p. 33,080-83.

[535] See id. at p. 33,082

suggests that the Commission attempt to reach agreement with the states on this matter or ask Congress for any necessary statutory change. Citizens Utilities also argues that the Commission should not unbundle the interstate transmission aspect of buy-sell transactions. It says that, unlike the analagous gas contracts, buy-sell arrangements on the electric side are not an end run around clear federal jurisdiction. Further, it argues that it would be very difficult to define those buy-sell transactions that truly belong under federal jurisdiction.

IL Com also objects to the NOPR's characterization of buy-sell transactions. It argues that the fact that a transaction becomes unbundled does not suddenly make part of it under federal jurisdiction. Nucor argues that there is no need for the Commission to resolve this issue now; it suggests that the buy-sell arrangement is only tangentially related to open access. It argues that each buy-sell transaction will have to be addressed individually.

UT Com seeks clarification as to what the Commission means by buy-sell arrangements:

we currently authorize interruptible "buy-through" contracts, through which a retail customer, taking service subject to interruption for either economic or technical reasons, can opt to "buy-through" an interruption. The public utility purchases energy on behalf of the customer and sells it at cost to the customer. In our opinion, such transactions are not an example of a buy-sell transaction within the meaning of the proposed rule.[536]

DOD objects to the statement in the NOPR that "buy-sell" transactions are not really bundled retail service. It says that this

[536] UT Com Initial Comments at p. 4-5.

view will discourage the development of innovative state progmms, such as direct access programs. NYSEG also argues that buy-sell transactions are not under the Commission's jurisdiction. It argues that these transactions are unlike buy-sell transactions on the gas side, where the Commission asserted jurisdiction to prevent LDCs from circumventing the nondiscrimination standard it imposed on the release of capacity. NYSEG says:

In contrast to its regulation of gas buysells. if the Commission regulates electric buy-sell transactions it would forego regulation of a transaction in which the Commission has a significant interest (i.e., access to the upstream seller's transmission), to regulate a transaction in which the Commission has virtually no interest (i.e.. access to the distributing utility's system). Electric utilities must serve each retail customer irrespective of whether the customer takes traditional bundled service or retail buy–sell service. Unlike excess upstream gas pipeline capacity, the capacity on the local utility's electric system would not be allocated to another customer in a FERC jurisdictional transaction absent the electric buy-sell transaction. Electric buy-sell transactions are not designed so as to manipulate the assignment of upstream transmission capacity. Consequently, the impetus for FERC to reclassify gas buy-sell transactions as capacity assignments is not present in the electric context.[537]

NYSEG argues that there are only two possible grounds for the Commission's assertion of jurisdiction over electric buy-sell transactions: either (1) the sale for resale by the supplier is really a sale at retail to the end user, and the resale by the local utility is really unbundled retail wheeling); or (2) the Commission has jurisdiction over transmission service that is part of bundled

[537] NYSEG Initial comments at p. 48 (footnote omitted).

retail service. It claims that the second ground is invalid because the transmission aspect of bundled retail service is distribution. It also claims that the first ground is invalid because it assumes that the sale by the supplier to the local utility is not a sale for resale even though the contract says that it is. NYSEG states:

> The logical outcome would be that FERC would not have jurisdiction over the sale by the supplier to the utility, including transmission by that supplier because it would be a bundled retail sale. This is because, if the commission holds the resale to be a retail wheel, then it would have to find that the sale by the supplier is a retail sale to the end user. The Commission cannot at once regulate the sale for resale and the "retail transmission service."The Commission would regulate the transmission rates of the local franchise utility, although it would not regulate the access to such transmission service—a matter FERC leaves to state regulators. In the process, FERC would abandon the ability to regulate access to the supplier's bundled "retail power sale and transmission service," a transaction that FERC arguably has an interest in regulating.[538]

Finally, NYSEG argues that if the Commission insists on asserting jurisdiction, it should at least grandfather existing contracts.

UT industrials state that where there is a state barrier to a buy-sell transaction, the Commission should allow the utility to file a tariff with the Commission that would permit the utility to complete a voluntary buy-sell transaction as the NOPR proposes. However, it contends that when a state regulatory authority is authorized to, and has approved buy-sell transactions, it is not necessary for the Commission to become

---

[538] NYSEG Initial Comments at p. 50.

involved. It urges the Commission to allow such transactions to take place free of Commission regulation. Commission Conclusion.

In the discussion below, the Commission addresses the following jurisdictional issues raised in the prior NOPRs:

a. Does the Commission have jurisdiction over unbundled transmission in interstate commerce by a public utility when such transmission is used to transport electric energy that is sold to an end user?

b. If so, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to an end user?

c. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to a purchaser who will then re-sell the energy to an end user?

d. What procedures are appropriate for making jurisdictional determinations?

In addition, the Commission addresses concerns raised by state regulators which indicate that competition and open access are perceived as threatening the traditional regulatory functions of state commissions. The Federal Power Act differentiates between state and federal regulation of electric power. As we discuss below, the Commission believes that any change in state or federal jurisdiction over physical transmission assets and related costs will not affect the traditional tasks of state and federal regulators.

The wide range of jurisdictional interpretations and proposals in the comments reflects the fact that the legislative history of the FPA and case law interpreting federal/state jurisdiction under that Act and the Natural Gas Act grew out of a market structure in which electricity and transmission generally were bought and sold on a bundled basis. As a result, most transactions included either a retail or wholesale sale of electric energy and jurisdictional lines were drawn on the basis of this sale. Thus, the cases simply do not resolve dispositively these jurisdictional issues when they arise in the context of the market structures and unbundled transactions being contemplated in today's electric industry. However, after reviewing the extensive analysis of the FPA, legislative history, and case law contained in both our initial Stranded Cost NOPR and in our Open Access NOPR, and the comments received on that analysis, we continue to believe that we were correct in asserting jurisdiction over the transmission component of an unbundled interstate retail wheeling transaction. We therefore reaffirm our conclusion. We also reaffirm and clarify our determinations regarding the tests to be used to determine what constitute Commission-jurisdictional transmission facilities and what constitute state-jurisdictional local distribution facilities in situations involving unbundled wholesale wheeling and unbundled retail wheeling.[539]

At the same time, the" Commission strongly supports the efforts of states to pursue pro-competitive policies. We recognize that jurisdictional issues raise overlapping Federal and state policy concerns that call for heightened cooperation among federal and state regulators. As discussed below, where states unbundle retail sales, we will give deference to their

[539] Not only do we conclude that our determinations are legally supportable under the case law, but we believe it is imperative to provide guidance to public utilities and state regulators as to our position on where the jurisdictional boundaries lie.

determinations as to which facilities are transmission and which are local distribution, provided that the states, in making such determinations, apply the seven criteria discussed in the NOPR and reaffirmed below. In addition, we clarify our view that there is an element of local distribution service in any unbundled retail transaction, and further clarify other aspects of our jurisdictional ruling to preserve state jurisdiction over matters that are of local concern and will remain subject to state jurisdiction if retail unbundling occurs.

We first address our legal determination that if unbundled retail transmission in interstate commerce occurs voluntarily by a public utility or as a result of a state retail access program, this Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission. No commenter has raised cases or legislative history not previously considered in our prior NOPRs, and we will not repeat here our full legal analysis of this issue.[540] However, we find compelling the fact that section 201 of the FPA, on. its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.[541] Unlike our jurisdiction over sales of electric energy, which section 201 of the FPA specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission.

[540] The Commission's complete legal analysis on this issue, and on the related issue of what facilities are Commission-jurisdictional transmission facilities, and what are state jurisdictional local distribution facilities, are contained in Appendix G to this Rule.

[541] Section 201(b)(1) specifically exempts from Commission jurisdiction facilities used for transmission in intrastate commerce and transmission of electric energy consumed wholly by the transmitter. As a result, we have no jurisdiction over retail wheeling that occurs in Alaska, Hawaii and the Electric Reliability Council (ERCOT) portion of Texas since transactions in those areas are intrastate.

In response to those commenters (including NARUC) who argue that the Commission did not explain why its authority attaches only to unbundled, but not bundled, retail transmission in interstate commerce by public utilities, we believe that when transmission is sold at retail as part and parcel of the delivered product called electric energy, the transaction is a sale of electric energy at retail. Under the FPA, the Commission's jurisdiction over sales of electric energy extends only to wholesale sales. However, when a retail transaction is broken into two products that are sold separately (perhaps by two different suppliers: an electric energy supplier and a transmission supplier), we believe the jurisdictional lines change. In this situation, the state clearly retains jurisdiction over the sale of the power. However, the unbundled transmission service involves only the provision of "transmission in interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission. Therefore, when a bundled retail sale is unbundled and becomes separate transmission and power sales transactions, the resulting transmission transaction falls within the Federal sphere of regulation.

In asserting jurisdiction over unbundled retail transmission in interstate commerce by public utilities, the Commission in no way is asserting jurisdiction to order retail transmission directly to an ultimate consumer. Section 212(h) of the FPA clearly prohibits us from doing so. In addition, as stated in both the initial Stranded Cost NOPR and the Open Access NOPR, we do not address whether states have authority to order retail wheeling in interstate commerce. The Commission's assertion of jurisdiction is that if retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

The Commission clarifies that nothing in this jurisdictional determination changes historical state franchise areas or interferes with state laws governing retail marketing areas of electric utilities: Section 212(g) of the FPA prohibits Commission orders that would be inconsistent with such laws. However, we reject arguments made by some of the commenters that section 212(g) could somehow be construed to give states authority over the rates, terms, and conditions of unbundled interstate transmission within retail marketing areas.[542] While our jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or nonexclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over transmission in interstate commerce by public utilities.

In response to several of the commenters, we further clarify that the Commission's jurisdiction over the rates, terms, and conditions of unbundled retail transmission is no broader than our authority over transmission used for wholesale transactions; and will not affect matters otherwise left to the states by

---

[542] The legislative history of FPA section 212(g) and its predecessor, former section 211(c)(3), indicates that the provision was focused on not interfering with state laws governing retail service territories and not permitting Commission wheeling orders "for purposes of sale by a utility to an ultimate consumer who is within the service territory of another utility (other than the applicant) where such territory is established by or under State law, rule, or decision," See H.R. Conf. Rep. No. 1750, 95th Cong., 2d Sess. 92 (1978), reprinted in 1978 U.S. Code Cong. & Ad. News 7797, 7826. Nothing on the face of section 212(g) or the legislative history of either the Energy Policy Act or PURPA indicates that the provision in any way affects the Commission's authority over rates, terms, and conditions of transmission in interstate commerce by public utilities.

Congress.[543] The Federal Power Act recognizes that retail marketing areas are governed by state law. Moreover, we believe that states have authority over the service of delivering electric energy to end users. In exercising this authority, state regulatory commissions and state legislatures have traditionally developed social and environmental programs suited to the circumstances of their states. State regulation of most power production and virtually all distribution and consumption of electric energy is clearly distinguishable from this Commission's responsibility to ensure open and non-discriminatory interstate transmission service. Nothing adopted by the Commission today, including its interpretation of its authority over retail transmission or how the separate distribution and transmission functions and assets are discerned when retail service is unbundled, is inconsistent with traditional state regulatory authority in this area.

The Commission reiterates its strong interest in preventing any balkanization of the interstate power market. Although the Commission believes its Final Rule will accommodate retail competition, if it is offered voluntarily by a utility or ordered by a state, our policies relate only to the bulk power market and not traditional state regulation of the retail market.[544]

---

[543] Among other things, Congress left to the States authority to regulate generation and transmission siting. See FPA sections 201(b) and 211(d)(1); Section 731 of the Energy Policy Act.

[544] This Final Rule will not affect or encroach upon state authority in such traditional areas as the authority over local service issues, including reliability of local service; administration of integrated resource planning and utility buy-side and demand-side decisions, including DSM; authority over utility generation and resource portfolios; and authority to impose non-bypassable distribution or retail stranded cost charges.

NARUC has requested that the Commission specifically clarify in §35.27 of its proposed rules[545] that nothing in our final rule limits the authority of a state commission "to allow or disallow the inclusion of the costs of electric energy purchased at wholesale in retail rates subject to such State commission jurisdiction." We will adopt NARUC's proposal with modification, but add it as a separate subsection. The Final Rule adopts a new § 35.27(b) as follows:

Nothing in this part (i) shall be construed as preempting or affecting any jurisdiction a state commission or other state authority may have under applicable state and federal law, or (ii) limits the authority of a state commission in accordance with state and federal law to establish (a) competitive procedures for the acquisition of electric energy, including demand-side management, purchased at wholesale, or (b) non-discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

With respect to the Commission's adoption of the Open Access NOPR's functional/technical tests for determining what facilities are Commission-jurisdictional facilities used for transmission in interstate commerce and what facilities are state-jurisdictional local distribution facilities, the case law supports a bright line for unbundled wholesale transmission, i.e., transmission of electric energy that is being sold for resale. This is consistent with the bright line drawn by Congress to fill the Attleboro gap for regulating wholesale sales of electric

---

[545] Section 35.17 of the proposed rules provided that any public utility seeking authorization to engage in sales for resale at market-based rates shall not be required to demonstrate any lack of market power in generation with respect to sales from capacity first placed in service on or after 30 days from the date of publication of the Final Rule in the Federal Register. *FERC Statutes and Regulations*, ¶32,514 at p. 33,154.

energy. The case law also supports a bright line with respect to retail transmission by intervening utilities. i.e., transmission by those utilities between the new retail generation supplier and the public utility that previously provided bundled retail service to the end user. However, despite many commenters' arguments to the contrary, we cannot define such a bright line for unbundled retail transmission by the public utility that previously provided bundled retail service to the end user. In fact, the limited case law, including CL&P and Colton, supports a case-by-case determination.[546] Accordingly, we believe our technical test, with its seven indicators, will permit reasoned factual determinations in individual cases.

Although we are unable to draw the bright line for local distribution facilities that many commenters would like, we believe it is important to make two clarifications regarding local distribution in the context of retail wheeling. First, even when our technical test for local distribution facilities identifies no local distribution facilities for a specific transaction, we believe that states have authority over the service of delivering electric energy to end users. Second, through their jurisdiction over retail delivery services, states have authority not only to assess stranded costs but also to assess charges for stranded benefits, such as low-income assistance and demand-side management. Because their authority is over services, not just the facilities, states can assign stranded costs and benefits based on usage (kWh), demand (kW), or any combination or method they find

[546] As noted, the Commission's detailed legal analysis is contained in Appendix G. We are particularly persuaded by the Supreme Court's statement that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. See CL&P, 515 U.S. at p. 534-35.

appropriate. They do not have to assign them to specific facilities.[547]

Thus, while we believe in most cases there will be identifiable local distribution facilities subject to state jurisdiction, we also believe that even where there are no identifiable local distribution facilities. states nevertheless have jurisdiction in all circumstances over the service of delivering energy to end users. Under this interpretation of state/federal jurisdiction, customers have no incentive to structure a purchase so as to avoid using identifiable local distribution facilities in order to bypass state jurisdiction and thus avoid being assessed charges for stranded costs and benefits.

Based on concerns raised by state commissions as well as some utilities, we have further determined that it is appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs. We also believe it is important to develop mechanisms to avoid regulatory conflict and to help provide certainty to utilities as to which regulator has jurisdiction over which facilities. These are discussed below.

Determining where to draw the jurisdictional line for facilities used in unbundled retail wheeling transactions will involve case-specific determinations that evaluate the seven local distribution indicators that we are adopting. We believe that the Commission should take advantage of state regulatory authorities' knowledge and expertise concerning the facilities of the utilities that they regulate. Therefore, in instances of unbundled retail wheeling that occurs as a result of a state retail

[547] As noted above, states retain authority over state integrated resource planning, utility resource portfolios, and utility buy-side and demand-side decisions.

access program, we will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[548] Moreover, we recognize that in some cases the Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

Some commenters have asked the Commission to provide a forum to prevent or resolve disputes over the correct classification of facilities as transmission or local distribution. As a means of facilitating jurisdictional line-drawing, we will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the principles established in the Final Rule, the Commission will defer to such classifications and/or cost allocations.[549] We

---

[548] In order to give such deference, we expect state regulators to specifically evaluate the seven indicators and any other relevant facts and to make recommendations consistent with the essential elements of the Rule.

[549] This should also alleviate some concerns about the potential for costs not being accounted for if the Commission and a state commission use different methods of allocating costs.

encourage public utilities and their state regulatory authorities to attempt to agree to utility-specific classifications and allocations that the utility may file at the Commission.

A number of commenters have asked the Commission to defer to state commission recommendations or decisions regarding rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities. Some have suggested that we set broad guidelines for such rates, terms, and conditions, and then allow states to actually implement the guidelines. While the Commission cannot simply turn over its jurisdiction for the states to implement, we understand the concerns raised by many state regulators and believe that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances. as discussed below.

As we determined in the NOPR, when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes—a transmission component and a local distribution component. The Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component.[550] Thus, the rates, terms, and conditions of unbundled retail transmission by a public utility must be filed at the Commission. When this occurs, we will generally expect unbundled retail wheeling customers to take service under the same FERC tariff that applies to wholesale customers. However, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a

---

[550] As discussed above, even if there were instances where no local distribution facilities are used, we believe states have authority over the service of delivering electric energy to end users.

separate retail transmission tariff[551] to accommodate the design and special needs of such programs. In such situations, the Commission will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by this Final Rule. In addition, rates must be consistent with our Transmission Pricing Policy Statement. and the guidance herein concerning ancillary services.[552]

A final jurisdictional issue raised in the Open Access NOPR concerns buy-sell transactions. We remain concerned, just as we were with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, we reaffirm our conclusion that we have jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. However, we recognize that there is a wide range of programs and transactions that might or might not fall within this category. We will address these on a case-by-case basis.

In summary, the Commission reaffirms and clarifies its prior jurisdictional conclusions and tests for determining the demarcation between federal and state jurisdiction over transmission in interstate commerce and local distribution. We

---

[551] *I.e.*, the tariff would be different from the tariff that applies to wholesale customers. Such tariff would still be filed with the Commission under FPA section 205.

[552] In applying the principles of the Final Rule to retail transmission tariffs, the Commission clearly cannot order retail wheeling directly to an ultimate consumer. See FPA section 212(h).

have attempted to address these issues in a way that provides for flexibility and recognition of legitimate state concerns. With regard to retail services, we recognize the states' concerns that the unbundling of retail transactions would result in changes from what historically has been regulated by the states (principally, the rates of transmission assets previously included in retail rate base). However, the decision to provide unbundled retail wheeling is not the Commission's to make because we have no authority to order transmission directly to an ultimate consumer. In addition, even if a retail access program occurs, we do not believe the unbundling of retail transactions will radically change fundamental state authorities, including authority to regulate the vast majority of generation asset costs, the siting and maintenance of generation facilities and transmission lines, and decisions regarding retail service territories. Further, the Commission intends to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies. As the electric industry and state regulatory authorities continue to develop new competitive market structures and consider retail wheeling programs, we believe that the tests and mechanisms we have provided in this Rule will accommodate both Federal and state interests and will help provide jurisdictional certainty to market participants.

J. *Stranded Costs*

1. Justification for Allowing Recovery of Stranded Costs

In the Supplemental Stranded Cost NOPR, the Commission noted that the Open Access Rule would give a utility's historical wholesale customers greatly enhanced opportunities to reach new suppliers.[553] This would affect the way in which utilities

---

[553] *FERC Statutes and Regulations* ¶ 32,514 at p. 33,095.

have recovered costs under the traditional regulatory system that, on the one hand, imposed an obligation to serve,[554] and, on the other hand, permitted recovery of all prudently incurred costs. We noted that if customers leave their utilities' generation systems without paying a share of these costs, the costs will become stranded unless they can be recovered from other customers. The Commission stated in the NOPR that we must address the costs of the transition to a competitive industry by allowing utilities to recover their legitimate, prudent and verifiable stranded costs simultaneously with any final rule we adopt requiring open access transmission.[555]

Virtually all of the investor-owned utility commenters as well as commenters representing state commissions and other constituencies support the NOPR's premise that stranded costs can be created when a customer switches suppliers. They endorse the proposal to allow the recovery of legitimate and verifiable stranded tract, or a customer is seeking to shorten or eliminate the term of an existing contract, we believe that each have a heavy burden in demonstrating that the contract ought to be modified. Still, we believe that given the industry circumstances now facing us, both selling utilities and their customers ought to have an opportunity to make the case that their existing requirements contracts ought to be modified. By providing both buyers and sellers this opportunity, the Commission attempts to strike a reasonable balance of the interests of all market participants. The Commission expects that many of the arguments presented by buyers and sellers in such proceedings will be fact specific.

---

[554] The supplemental Stranded Cost NOPR described such an obligation as explicit at retail and arguably implicit at wholesale, *FERC Statutes and Regulations* ¶ 32,514 at p. 33,101.

[555] Id. at p. 33,095-96, 33,10.1

c. Transition Period

We reaffirm our proposal to allow a public utility or its customer to file a proposed stranded cost amendment, or to allow a public utility or transmitting utility to file a proposal to recover stranded costs through a departing generation customer's transmission rates, at any time prior to the expiration of the contract. There is no uniform time remaining on requirements contracts executed on or before July 11, 1994. Any limitation on the period in which parties could propose amendments covering stranded costs (e.g., 3 years) would thus unequally affect market participants. Those with long terms remaining on their contracts could object that immediately addressing the issue would not be cost effective. For example, a utility with a long remaining term (e.g., 20 years) might not even seek stranded cost recovery depending on the competitive value of its assets near the end of the contract term.[691] However, such a utility would invariably seek to preserve its option to seek stranded cost recovery if its failure to do so within a short period resulted in a waiver of its right to do so. 6. Recovery of Stranded Costs Caused by Retail-Turned-Wholesale Customers

In the Supplemental Stranded Cost NOPR, we stated that both this Commission and state commissions have the legal authority to address stranded costs that result from retail customers becoming wholesale customers who then obtain transmission under the open access tariffs.[692] We proposed that this Commission should be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers, We explained that if a retail customer becomes a legitimate wholesale customer (such as through municipalization),

---

[691] The value of its assets could vary over time as new technologies emerge, fuel costs fluctuate, or environmental requirements change.

[692] *FERC Statutes and Regulations* ¶ 32,514 at p. 33,127.

it becomes eligible to use the non-discriminatory open access tariffs:

> If costs are stranded as a result of this wholesale transmission access, we believe that these costs should be viewed as "wholesale stranded costs." But for the ability of the new wholesale entity to reach another generation supplier through the FERC-filed open access transmission tariff, such costs would not be stranded.[693]

We accordingly proposed to define "wholesale stranded costs" to include stranded costs resulting from unbundled transmission for newly-created wholesale customers and sought comments on this definition.

We proposed to require the same evidentiary demonstration for recovery as that required if recovery were sought from a wholesale requirements customer. We reaffirmed our proposal in the initial Stranded Cost NOPR that a utility will have to show that the stranded costs are not more than the net revenues that the retail-turned-wholesale customer would have contributed to the utility had it remained a retail customer of the utility, and that the utility has taken and will take reasonable steps to mitigate stranded costs. We further proposed to deduct any recovery that a state has permitted from departing retail-turned-wholesale customers from the legitimate stranded costs of which we will allow recovery. In addition, we proposed to apply the same procedures for obtaining an estimate of maximum stranded cost exposure without mitigation to retail customers contemplating becoming wholesale transmission customers as those proposed for wholesale customers.[694]

---

[693] Id. at p. 33,128.

[694] Id.

Some commenters contend that stranded costs that result when a retail customer becomes a wholesale customer should be left to the states as a matter of law and comity.[695] These commenters argue, among other things, that because the facilities used to provide retail service to these retail customers were subject to state jurisdiction and were included in retail rate base when the service was rendered, the state is the appropriate entity to determine the extent to which those customers should compensate the utility for the stranding of these costs. According to ELCON, "(a) retail customer's new found access to the wholesale market does not provide FERC with authority over costs that originated with the local distribution function."[696]

Commenters assert that stranded costs resulting from the creation of new wholesale entities will occur as a result of state or local decision making.[697] A number of commenters contend that in states where the state commission has control over municipalization, the Commission has no authority to provide for the recovery of stranded costs due to municipalization.[698] IL Com asserts that the Commission lacks authority over retail-turned -wholesale stranded costs, even in the absence of

---

[695] *E.g., NARUC, ELCON, TAPS, NASUCA, N.Y.* Mayors, NY Industrials, American Iron & Steel, Missouri Joint Commission, Omaha PPD, MI Com, NYU Com, NJ BPU, VT DPS, OK Com, IN Com, UT Com,WA Com, Environmental Action, IN Industrials, LA DWP, Seattle, CAMU, Las Cruces, UT Industrials, Suffolk County, NM Industrials, CO Consumers Counsel.

[696] ELCON Comments, dated July 25, 1995, at p. 41.

[697] *E.g.*, MD Com, MI Com, LA DWP, Las Cruces. For example, MD Com states that while open access transmission may make municipalization more attractive, it ultimately is MD Com's approval that makes municipalization possible in Maryland.

[698] *E.g.*, MD Com, Las Cruces, Caparo, Coalition on Federal-State Issues, IN Com, MI Com, Iowa Board.

any explicit statutory authority for state commissions to address such costs. FL Com argues that the Commission should address the recovery of these, stranded costs only upon petition from a state public utility commission.

According to some commenters, the availability of open access transmission tariffs does not convert the character of the costs of stranded generation that was built to serve retail customers from retail to wholesale.[699] CA Com argues that this reasoning could require the Commission to act as the primary forum for stranded costs resulting from retail wheeling if the Commission's jurisdiction over retail transmission is upheld. It argues that in such a case, there also would be a relationship between the Commission-jurisdictional transmission and stranded costs.

Some commenters also submit that the potential for retail customers to become wholesale customers has existed since the beginning of the industry and that utilities have had ample opportunity to adjust to this risk[700] A number of commenters submit that state commissions are in a better position than the Commission to address the recovery of costs that were incurred to serve retail customers and to take into consideration local concerns.[701]

---

[699] *E.g.*, IL Com, CA Com, Midwest Commissions, CO Consumers Counsel.

[700] *E.g.*, LA DWP, Ohio Manufacturers, MMWEC, American Iron & Steel, UT Industrial, MI Com, NY Industrials, WA Com, Caparo.

[701] *E.g.*, American Iron & Steel, MD Com, LA DWP, Suffolk County, MI Com, NJ BPU, N.Y. Mayors. NASUCA cites practical problems posed by the Commission's proposal to assume jurisdiction over stranded costs resulting from municipalization, such as how the Commission would transfer the revenues extracted from the retail-turned-wholesale customer to a non-wholesale, locally-franchised entity.

NARUC recognizes that a "practical regulatory gap may exist that prevents (state commission) consideration of recovery of *** potentially stranded costs" in certain instances "such as municipalization and cooperatives, where retail customers become wholesale customers under a FERC-approved open access tariff, (and) costs of the utility which served the customer at retail may become stranded."[702] NARUC proposes that the affected states and the Commission collaboratively develop mechanisms (which may involve amendments to the FPA, state statutes. or both) to eliminate these regulatory gaps.

Some commenters object that the Commission's proposal to be the primary forum for recovery of stranded costs caused by retail-turned-wholesale customers would make municipalization more expensive and therefore would discourage municipalities from seeking alternative sources of electricity.[703] Some argue that different treatment of stranded costs between federal and state authorities may lead to forum-shopping as a primary determinant in the decision to municipalize.[704]

A number of commenters also suggest that the NOPR is inconsistent with prior Commission treatment of municipalization because the Commission has historically promoted franchise competition between municipalities and utilities and has never before suggested that utilities could "penalize" municipalization decisions through generation cost

---

[702] NARUC Initial Comments at p. 18-19.

[703] *E.g.*, N.Y. Mayors, NIEP, Wing Group, VT DPS, NY Industrials, American Iron & Steel, Environmental Action, IN Industrials, Las Cruces, Caparo,UT Industrials.

[704] *E.g.*, In Com.

add-ons to transmission rates.[705] VT DPS states: "By the Commission's logic, there would never have been an Otter Tail case. If Otter Tail could have made a stranded cost claim against the municipal utility Elbow Lake planned to create, Otter Tail would never have needed to refuse to wheel."[706]

Suffolk County states that the Commission already considered stranded costs in the context of retail-turned-wholesale customers in United Illuminating Company,[707] where the Commission required United Illuminating to remove a provision in its proposed transmission tariff that would have allowed it to recover stranded costs associated with former retail loads served by new municipal systems. Suffolk County states that the Commission made clear that stranded cost matters, including those caused by municipalization, properly would be raised before state regulatory authorities. It objects that the Open Access NOPR ignores this case. Suffolk County also submits that the Commission's adoption of the settlement approved by the Massachusetts DPU in the Massachusetts Bay Transportation Authority case should serve as an example of proper jurisdictional deference with respect to local issues.[708]

---

[705] *E.g.*, VT DPS, American Iron & Steel, American Forest & Paper states that allowing stranded cost recovery in the event of municipalization would be inconsistent with the Commission's actions in the natural gas industry, where the Commission has encouraged competition at the retail level (through competitive bypass, rather than franchise competition) and has not imposed transition charges or exit fees on converting customers.

[706] VT DPS Intitial Comments at p. 49: see also American Iron & Steel, NY Industrials, Caparo.

[707] 63 FERC ¶61,212 (1993), reh'g denied, 64 FERC ¶61,087 (1993)

[708] See Massachusetts Electric Company, 68 FERC ¶ 61,101 (1994): Letter Order dated March 3, 1995, Docket No. ER94-129-000 (approving settlement).

However, many other commenters support the Commission's proposal to be the primary forum for retail-turned-wholesale stranded costs.[709] These commenters submit, among other things, that the Commission's jurisdiction over such costs is clear.[710] Coalition for Economic Competition states that when a utility's costs are stranded through the availability of Commission-jurisdictional transmission service, the Commission must address those costs. It argues that commenters opposing the Commission's jurisdiction fail to analyze the Commission's duty to establish just and reasonable rates for Commission jurisdictional transmission service.

A number of commenters support the Commission's proposal to address retail- turned-wholesale stranded costs on the basis that many state commissions either lack authority to address costs that are stranded because of expanding or newly created municipal systems, or have failed to address such costs.[711] El

---

[709] *E.g.*, EEI, PSE&G, Centerior, Com Ed Consumers Power, Detroit Edison, Duke, El Paso, Energy, LILCO, Minnesota Power, Montana-Dakota Utilities, NYSEG, PECO, PG&E, PSNM, Southern, Utilities for Improved Transition, Allegheny, OH Com, Utilicorp, PA Com, WI Com, Coalition for Economic Competition, Central Louisiana, United Illuminating, Utility Investors Analysis, Nuclear Energy Institute, Utility Shareholders.

[710] *E.g.*, Consumers Power, Coalition for Economic Competition, Utilities For Improved Transition.

[711] *E.g.* Detroit Edison, Minnesota Power, El Paso, LILCO, Centerior, PG&E, PG&E urges a clarification in the rule so that the Commission would address retail-turned-wholesale stranded costs only if the state commission either lacks jurisdiction over municipal utilities, or, if it has jurisdiction, declines to address stranded costs. Where a state commission possesses jurisdiction over municipal entities and provides a utility with stranded cost recovery from former retail customers that have municipalized, PG&E proposes that such action should be final and not subject to Commission review. Other commenters, such as El Paso, ask the Commission to establish itself as the forum of last resort when states do not provide for full recovery of stranded costs.

Paso adds that any protection offered by state judicial condemnation proceedings does not obviate the need for the Commission's involvement in this issue, noting that condemnation awards may not provide full stranded investment recovery under the Commission's standards. In addition, El Paso suggests that municipalization may occur through means other than condemnation of the distribution systems of electric utilities, such as when a municipality constructs its own, duplicative distribution facilities.

Several commenters also indicate that by forthrightly addressing this issue, the Commission has removed a cloud of uncertainty that would have taken years to resolve through litigation.[712] El Paso states that the proposed rule is needed because utilities may be subject to stranded costs resulting from municipalization in two separate state jurisdictions.

In response to the argument that stranded costs are exclusively subject to state jurisdiction, SoCal Edison asserts that whether the costs are retail or wholesale is irrelevant because the issue is how and where these costs should be recovered. According to SoCal Edison, if the Commission finds that these costs are just and reasonable costs associated with providing open access transmission service, the Commission may allow utilities to recover them in Commission-regulated rates.

Coalition for Economic Competition notes that while utilities are aware of state laws allowing municipalities to condemn electric facilities and to form utilities, in recent decades, it has not happened on most systems. Moreover, it argues that merely being on notice that municipalization is a possibility does not relieve utilities of their state-imposed obligation to serve all customers in their franchise areas. It asserts that utilities had to

---

[712] *E.g.* Coalition for Economic Competition, El Paso.

continue to invest in plant to satisfy their duty to serve. In addition, it submits that utilities had a reasonable expectation that they would continue to serve retail load because, among other things, state regulators set long amortization periods of 30-40 years for depreciation rates.

Some commenters state that the Commission also should ensure that stranded costs are recovered when a municipal utility annexes territory served by another utility or otherwise expands its service territory.[713] A number of commenters also urge the Commission to ensure recovery of costs that are stranded if a municipal utility or a newly-formed wholesale or municipal utility physically interconnects to another utility or builds new transmission or distribution facilities to the municipal system.[714]

Several commenters believe that close coordination between the Commission and state regulators as to the calculation of stranded costs is important in the case of municipalization.[715] A number of state commissions suggest that the Commission allow the states to set the level of retail turned-wholesale

---

[713] *E.g.* EEI, Minnesota Power, Centerior, Public Service Co of CO, SoCal Edison, Coalition for Economic Competition, PG&E asks that we allow utilities to seek recovery at the Commission for stranded costs attributable to former retail customers that have become customers of existing public agencies or municipal utilities where such costs cannot be collected at the state level.

[714] *E.g.*, Centerior, Coalition for Economic Competition, PG&E. Coalition for Economic Competition proposes that the Commission accept just and reasonable regional stranded cost recovery mechanisms in such situations to enable regional transmission associations (whether through pool and interpool arrangements or regional transmission groups) to collect through Commission-filed rate schedules from interconnected utilities charges equal to the costs otherwise stranded as a result of Commission-jurisdictional service realignments.

[715] *E.g.*, SoCal Edison, OH Com, NY Com, MI Com, Coalition on Federal-State Issues.

stranded costs to be recovered in wholesale transmission rates set by the Commission.[716] They submit that this approach would respect state interests in controlling the rate impact of stranded costs, while allowing the Commission to design cost recovery, and would address the needs of industrial customers and other stakeholders by providing a forum before state regulators who will be more aware of their particular needs. Further, they contend that this approach would prevent relitigation of issues, minimize forum-shopping, and prevent legitimate and verifiable costs from falling through the cracks or being double-recovered.[717] NY Industrials asks the Commission to clarify that utilities will not be allowed to seek cost recovery at both the Commission and state commissions.

Commission Conclusion

We reaffirm our preliminary determination that this Commission should be the primary forum for addressing the recovery of stranded Costs caused by retail-turned-wholesale customers. If such a customer is able to reach a new generation supplier because of the new open access (through the use of a FERC-filed open access transmission tariff or through transmission services ordered pursuant to Section 211 of the FPA), we believe that any costs stranded as a result of this wholesale transmission access should be viewed as "wholesale stranded costs." Such costs would not be stranded but for the action of this Commission (either through a mandatory FPA section 205-206 open access tariff or an order under FPA section 211) in permitting the new wholesale entity to become

---

[716] *E.g.*, MI Com, NY Com, Ohio Com.

[717] PG&E proposes a similar approach, noting that if there are differences in the stranded cost method used by the Commission and the states, an incentive may remain for retail customers to municipalize merely to take advantage of more favorable stranded cost treatment at the Comission.

an unbundled transmission services customer of the utility and thereby to obtain power from a new supplier.[718] There is a clear nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs. In these circumstances, we believe that this Commission should be the primary forum for addressing recovery of such costs. To avoid forum-shopping and duplicative litigation of the issue, we expect parties to raise claims before this Commission in the first instance.[719]

Some commenters have asked us also to be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory. We decline to do so because in these situations there is no direct nexus between the FERC-jurisdictional transmission access requirement and the

---

[718] Costs that are exposed to nonrecovery when a retail customer or a newly-created wholesale power sales customer ceases to purchase power from the utility and does not use the utility's transmission system to reach a new generation supplier (e.g., through self-generation or use of another utility's transmission system) do not meet the definition of "wholesale stranded costs" for which this rule provides an opportunity for recovery. Such costs are outside the scope of this rule because such costs would not be stranded as a result of the new open access. See Section IV.J.12.

[719] We recognize that we took a different approach to retail-turned-wholesale stranded cost recovery in United Illuminating, where we suggested that state and local regulatory authorities or the courts should be able to provide an adequate forum to address retail franchise matters, including recovery of stranded costs caused by municipalization, but said we would consider revisiting the question if United Illuminating could demonstrate the lack of a forum, 63 FERC at p. 62,583-84. Since the issuance of that decision, however, we have had an opportunity to reanalyze the nature of the stranded cost problem in cases where a retail customer becomes a wholesale customer, including the potential that there might not be a state regulatory forum for recovery of such costs. In these circumstances, we have determined that where such costs are stranded as a result of wholesale open access transmission, these costs should be viewed as wholesale stranded costs and this Commission should be the primary forum for addressing their recovery.

exposure to non-recovery of prudently incurred costs. The risk of an existing municipal utility expanding its territory was a risk prior to the Energy Policy Act and prior to any open access requirement.

Nevertheless, we are concerned that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission—either this Commission or state commissions—to address recovery of stranded costs.[720] We reserve the right to address such situations on a case-by-case basis.

As we indicated in the Supplemental Stranded Cost NOPR, if the state has permitted any recovery from departing retail-turned-wholesale customers (for example, if it imposed an exit fee prior to, or as a condition of, creating the wholesale entity), that amount will not, in fact, be stranded, and we will deduct that amount from the legitimate stranded costs for which we will allow recovery.

As discussed in Section IV.J.8-IV.J.9, we will require the same evidentiary demonstration for recovery of stranded costs from a retail-turned-wholesale customer, and will apply the same procedures for determining stranded cost obligation, as that required in the case of a wholesale requirements customer.

---

[720] The CA Com has asked that, "(t)o the extent of FERC's authority, it should assume jurisdiction to fulfill a backstop role in case retail customers evade a state-determined transition charge by becoming retail customers of an entity not subject to the state regulatory commission's jurisdiction. In assuming jurisdiction, the Commission should defer to the state commission's determination and allocation of stranded costs for the departing retail customer." CA Com March 18, 1996 Response to Supplemental Comments of PG&E.

7. Recovery of Stranded Costs Caused by Retail Wheeling

In the Supplemental Stranded Cost NOPR, we stated that both this Commission and state commissions have the legal authority to address stranded costs that result from retail customers who obtain retail wheeling from public utilities in order to reach a different generation supplier.[721] Because the vast majority of commenters urged the Commission not to assume responsibility for retail stranded costs, except in certain circumstances, we preliminarily concluded that it is appropriate to leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. We proposed to entertain requests to recover stranded costs caused by retail wheeling only when the state regulatory authority does not have authority under state law to address stranded costs at the time when the retail wheeling is required.[722] In so doing, we preliminarily accepted the view that stranded costs caused by retail wheeling are primarily a matter of local or state concern and thus, with the limited exception discussed above, generally must be recovered through retail charges.

---

[721] As discussed in Section IV.I, the Commission's authority to address retail stranded costs derives from its jurisdiction over the rates, terms and condition of unbundled transmission interstate commerce used by retail customers that obtain retail wheeling. The states' authority derives from state jurisdiction over local distribution facilities and over the service of delivering electric energy to end users, and from the authority to impose, among other things, retail exit fees and surcharges on local distribution rates.

[722] We proposed to require the same evidentiary demonstration for recovery of stranded costs from a retail customer that obtains retail wheeling as that required in the case of a wholesale requirements customer. We also reaffirmed our proposal in the initial Stranded Cost NOPR that a utility will have to show that the stranded costs are not more than the net revenues that the retail customer would have contributed to the utility had it remained a retail customer of the utility, and that the utility has taken and will take reasonable steps to mitigate stranded costs. *FERC Statutes and Regulations* ¶32,514 at p. 33,128.

We noted that the states have a number of mechanisms for addressing stranded costs caused by retail wheeling, one of which is a surcharge to state-jurisdictional rates for local distribution.[723] We encouraged the states to use the mechanisms available to them to address stranded costs.[724] We also noted that the states may use their jurisdiction over local distribution facilities to address "stranded benefits", such as environmental benefits associated with conservation, load management, and other demand side management programs.[725]

A number of commenters support the Commission's proposal for addressing stranded costs caused by retail wheeling.[726]

Other commenters urge the Commission to take a greater role in retail stranded cost recovery and to entertain requests to recover stranded costs as a backstop where: (1) State regulatory authorities have the authority to address stranded costs but either choose not to exercise that authority or fail to permit full

---

[723] As we noted in the Supplemental NOPR, a state may require payment of an exit fee before a franchise customer is permitted to obtain unbundled retail wheeling. If local distribution facilities are used by a retail wheeling customer, the state may allow recovery of stranded costs through rates for use of such local distribution facilities. In addition, as discussed in Section IV.I, because we believe that states have authority over the service of delivering electric energy to end users, not merely the local distribution facilities themselves, state authorities can assign stranded costs and benefits through a local distribution service charge, and may do so based on usage (kWh), demand (kW), or any combination or method they find appropriate. If a state decides not to take any of these routes, it may consider whether to allow recovery of stranded costs from remaining retail customers or whether shareholders should bear all or part of those costs. Id. at p. 33,129.

[724] Id. at p. 33,129-30.

[725] Id. at p. 33,0988 n.230.

[726] *E.g.*, Utilicorp, Houston L&P, PG&E, Freedom Energy Co. WI Com.

stranded cost recovery;[727] or (2) the state commission's authority is unclear.[728]

Commenters that support a greater Commission backstop role argue, among other things, that because the Commission has exclusive ratemaking jurisdiction over any stranded cost charges imposed "for or in connection with" interstate transmission service by public utilities, the Commission has an obligation to regulate the recovery of stranded costs from interstate retail transmission customers.[729] A number of these commenters argue that the determining factor is who has the jurisdiction to review the rates for the service, not who has the jurisdiction to order the service.[730] They explain that the Commission has jurisdiction over generating facilities and associated costs to the extent appropriate to establish just and reasonable rates for jurisdictional services. They disagree with other commenters who argue that only the jurisdiction under

---

[727] *E.g.*, EEI, EGA, Coalition for Economic Competition, Utilities for Improved Transition, Atlantic City, Arizona, Centerior, Com Ed, Detroit Edison, El Paso, LILCO, NU, NSP, NYSEG, United Illuminating, BG&E, Sierra Souther, UT Industrials, NRECA. NRECA argues that unless the Commission addresses stranded costs caused by retail wheeling where a state commission lacks authority, or has authority but decides not to exercise it, there could be a jurisdictional gap into which many rural electric cooperatives could fall.

[728] *E.g.*, CSW.

[729] *E.g.*, EEI, Illinois Power, PSNM, Entergy, Nuclear Energy Institute, Coalition for Economic Competition.

[730] *E.g.*, Coalition for Economic Competition, Illinois Power, Utilities for Improved Transition, EEI.

whose authority the costs were incurred and initially recovered should have authority to order recovery of stranded costs.[731]

These commenters contend that the Commission cannot abdicate its regulatory responsibilities by either deferring to the state commissions or otherwise failing to independently address the issue.[732] EEI and the Coalition for Economic Competition refer to "a long line of cases (where) the courts have held that where a federal regulatory agency * * * is charged with implementing a statutory framework, that agency is without authority to deviate from or abdicate its statutory responsibilities.[733] According to Coalition for Economic Competition. for example, the Commission could satisfy its obligation to address stranded costs that arise from retail wheeling by allowing states to determine retail stranded cost charges in the first instance; to the extent that the state allows full recovery. Coalition for Economic Competition submits that the Commission's obligation would be satisfied.

EEL asserts that it would be unduly discriminatory and preferential for the Commission to refuse to address all stranded costs arising from retail wheeling. According to EEL, the same arguments that support the Commission's decision to address costs that are stranded where retail load municipalizes and

---

[731] EEI notes, for example, that as use of electrical facilities shifts between retail and wholesale, jurisdiction over the rates to recover the allocated cost of service shifts between state commissions and this Commission, and that the regulatory authority is determined by the nature of the transactions and the classification of the customer, not the jurisdiction under which the costs originally arose.

[732] *E.g.*, Illinois Power, Utilities For Improved Transition, EEI, Coalition for Economic Competition.

[733] EEI Initial Comments at IV-13: see also Coalition for Economic Competition Initial Comments at p. 23-31.

where the state regulatory authority, at the time retail wheeling is required, lacks authority to act, apply with equal force to all other retail stranded costs. EEL submits that the nexus in these cases is that Commission-jurisdictional transmission service is the means by which the costs are stranded.[734]

Utility Working Group argues that the NOPR inappropriately characterizes the Commission's jurisdiction over retail stranded costs and that this could later be used against the Commission's exercise of its full authority. According to Utility Working Group, the NOPR depicts the Commission's jurisdiction as being derived from state law (in other words. the Commission will act where state regulatory authorities have no authority over retail stranded costs and will not act where state regulatory authorities have such authority). If the Commission desires to afford substantial deference to the states regarding retail stranded costs, Utility Working Group contends that the final rule should reflect that policy determination; however, the rule should not confuse policy with jurisdiction by purporting to place limits on, or attempting to waive, the Commission's jurisdiction over such costs.

Entergy asserts that the Commission's jurisdiction over multi-state utilities provides further support for our jurisdiction over retail stranded costs in certain contexts. Entergy states that most of the eleven multi-state registered holding company systems have some form of Commission-jurisdictional agreement that allocates production and transmission costs among the systems' affiliated operating companies. It asserts that these agreements by their very nature allocate costs among jurisdictions (that is, between states). Many of these agreements equalize the cost of generating reserves among affiliated operating companies, and such reserve equalization formulas

---

[734] See also SoCal Edison.

can shift retail stranded costs amorng states unless the Commission provides a regulatory forum to address cost-shifting. Citing Middle South Energy,[735] and City of New Orleans v. FERC,[736] Entergy submits that the Commission cannot sit on the sidelines when it comes to stranded retail costs on the Entergy system. According to Entergy, Commission and judicial precedent place on the Commission the responsibility to ensure that federally-approved costs and cost allocations are not undermined by state action.

Commenters also express concern that it will not be possible to be sure that a state regulatory authority has authority over retail stranded costs until after years of litigation. If the Commission waits for the resolution of challenges to state authority and a court holds that the state regulatory authority is without authority, these commenters assert that the bar on retroactive ratemaking could leave the states and the Commission without a remedy to compensate utilities for stranded costs.[737] A number of commenters suggest that while the states should be allowed to set retail wheeling stranded cost charges in the first instance, the Commission should accept filings to preserve a utility's ability to recover retail stranded costs from the time the customer departs if the state-authorized charges are not upheld in court. They submit that this would put customers on notice of the potential for Commission action and thereby avoid the retroactivity problem.[738]

---

[735] Opinion 234, 31 FERC ¶61,305, on reh'g, 32 FERC ¶61,425 (1985).

[736] 875 F.2d 903 (D.C. Cir. 1989), cert. denied sub nom. *Mississippi v. FERC*, 494 U.S. 1078 (1990).

[737] *E.g.*, NU, Coalition for Economic Competition, Illinois Power, EEI.

[738] *E.g.*, NEPCO, EEI, Coalition for Economic Competition Entergy.

Some commenters express concern that if the Commission does not take more decisive action on retail wheeling stranded costs, the result will be wasteful litigation that will discourage competition by causing financial uncertainty and higher financing costs for investor-owned utilities and higher rates for consumers.[739]Coalition for Economic Competition also asserts that stranded cost charges would be greatest at the start of a retail wheeling program, thereby making the years during which the state-authorized charges are subject to appeal more important for recovery purposes.

A number of commenters support Commission-established uniform standards for, and uniform recovery of, costs stranded as a result of open access to the interstate transmission system.[740] They argue that disparate state treatment of stranded costs would be economically inefficient and discriminatory and would burden interstate commerce.[741] Several commenters support state involvement in the establishment of uniform standards.[742]

In contrast to the commenters that support a greater Commission role in retail stranded cost recovery. NARUC and a number of other commenters oppose any Commission

---

[739] *E.g.*, LILCO, Coalition for Economic Competition.

[740] *E.g.*, NU, NSP, Illinois Power, Coalition for Economic competition, PSE&G, Utilities for Improved Transition, Philip Morris, EEI.

[741] Freedom Energy Co. rejects this argument on the basis that state regulation has never been wholly consistent and yet utilities have not asked for federal unification of state ratemaking policies or resolution of differences.

[742] *E.g.*, PSNM, GA Com, Omaha PPD, Illinois Power.

involvement in retail stranded costs.[743] These commenters contend, among other things, that the Commission lacks authority over these costs. Even if the Commission could assert such jurisdiction, they argue that as a policy matter it would be inappropriate for the Commission to delve into complicated legal and policy issues governed by varying state regulatory regimes.

According to some of these commenters,[744] section 201(a) of the FPA precludes an exercise of federal jurisdiction over retail stranded cost recovery because the Commission's jurisdiction extends "only to those matters which are not subject to regulation by the States."[745] NM Industrials argues that a lack of state commission authority is an affirmative state determination, either by act or omission, that stranded costs must be dealt with in a particular manner. It submits that the Commission also lacks authority over retail stranded costs when states either decide not to address such costs or, in the Commission's opinion, grant insufficient recovery of stranded costs. NM Industrials asserts that the language of the FPA and its legislative history indicate that Congress wanted to preclude Commission jurisdiction in those areas where states could exercise effective control, and that this limitation covers all matters which are or can be regulated by the states, including the recovery of stranded investment. NM Industrials also suggests that assertion of Commission jurisdiction would violate the

[743] *E.g.*, CA Com, MD Com, VA Com, IN Com, NH Com, NV Com, NY Com, OH Com, FL Com, AZ Com, TX Com, ELCON, NY Industrials, NY AG, NY Consumer Protection, MA DPU, Iowa Board, IN Industrials, Texas Industrials, NM Industrials, Reynolds, NYMEX, Legal Environmental Assistance, CO Consumers Counsel, NJ Ratepayer Advocate, IBM, ME Industrials, Jay, WEPCO, NH General Court.

[744] *E.g.*, NARUC, ELCOM, NY Industrials, NM Industrials, NV Com.

[745] 16 U.S.C. 824(a)

provision of section 212 of the FPA that prohibits the Commission from interfering with the states' authority over the transmission of energy directly to an ultimate consumer.[746]

Other commenters argue that the Commission's proposed treatment of retail stranded costs infringes on the states' jurisdiction over the allocation of costs that were under their jurisdiction when the costs were incurred. According to these commenters, the question of whether these costs should be recovered from other retail ratepayers, eliminated as excess capacity, or billed in some fashion to the customer now receiving wheeling service are purely questions of state ratemaking law.[747] Some commenters assert that. as a matter of policy, the Commission should stay out of retail stranded costs because only the states have sufficient knowledge and expertise regarding utility planning, investment, and forecasting to address these costs adequately.[748]

Commenters also express concern that the possibility of Commission involvement in retail stranded cost recovery will encourage forum-shopping whenever state commission action is unfavorable, even when states have procedures to deal with stranded costs. They argue that the result would be endless litigation over where federal jurisdiction ends and where state jurisdiction begins. They suggest that if a state fails to address retail stranded cost recovery, the issue should be addressed in

[746] See also *Freedom Energy Co. Reply Comments.*

[747] *E.g.*, ELCON, PA Com, NY Industrials, ND Com, VA Com, NM Com.

[748] *E.g.*, OH Com, NY Industrials, NM Com, IN Com, WA Com, NV Com, NY Com, Suffolk County, NY AG, Tonko, PA Industrials, NH General Court.

court or in state legislatures.[749] OH Cam contends that a Commission policy that does not recognize states' authority over retail stranded costs would be a disincentive for states to permit retail wheeling.

A number of commenters argue that recovery of retail stranded costs is not directly implicated by any Commission or Congressional action—that most such costs would be created by retail wheeling, which is not the subject of the Commission's open access initiatives—and thus need not be dealt with as part of the final rule.[750]

Commenters seek a number of clarifications concerning the Commission's position on, and the procedures for, retail stranded cost recovery. A number of commenters ask the Commission to clarify the states' role with respect to retail stranded cost recovery.[751] Others address the type of evidence required to establish that the State regulatory authority lacks authority to address stranded costs when retail wheeling is required.[752]

Several commenters express concern that customers receiving retail wheeling not be able to evade state stranded cost charges.[753] IL Com says that the Commission's proposal for determining whether facilities are state-jurisdictional "local

---

[749] *E.g.*, OH Com, PA Com, NM Com, CA Com, Blue Ridge.

[750] *E.g.*, Nucor, AEC & SMEPA.

[751] *E.g.*, NY Industrials, EGA, NJ BPU, Coalition on Federal-State Issues.

[752] *E.g.*, Iowa Board, Nevada Commission, CCEM: see also NE Public Power District.

[753] *E.g.*, IL Com, PG&E, Public Service Co. of CO.

distribution" facilities or Commission-jurisdictional "transmission" facilities in interstate commerce may not always, provide a state, with the opportunity to recover retail stranded costs through distribution rate surcharges. It says that the Commission does not offer any assurances that the case-by-case application of the proposed "functional-technical test" will result in a finding that "local distribution" facilities are used in all retail wheeling scenarios. PG&E asks the Commission to provide that all retail customers that opt for direct transmission access by definition take service over local distribution facilities and therefore may be subjected to a state-determined distribution rate that includes stranded cost surcharges.

A number of commenters ask the Commission to clarify that, in issuing the final rule, the Commission is not endorsing (either implicitly or explicitly) retail wheeling.[754]

Several commenters express concern that stranded costs may arise in one state jurisdiction and be shifted to another.[755] For example, MT Com says that an analysis confined to a state's boundaries may reveal no stranded costs, but that such costs may indirectly arise because of common pool revenue recovery mechanisms, which may be the largest source of stranded costs for some utilities. Entergy raises a similar concern in the context of holding company or other multi-state situations. It argues that denial of retail stranded cost recovery by a state regulatory authority could harm customers in other states. Entergy proposes that, while state regulators should be given the opportunity in the first instance to assure that stranded costs are recovered and are not shifted to other states, the Commission should allow utilities to file retail wheeling tariffs with the

---

[754] *E.g.*, NRECA, Wisconsin, EC, EEI, PECO, Missouri Basin Group.

[755] *E.g.*, MT Com, Entergy.

Commission to preserve the right to seek recovery from the Commission.

Several commenters oppose Entergy's proposal.[756] Among other things, they argue that the FPA does not authorize the Commission to act as an appellate court over retail regulators. They assert that, in the case of a multi-state holding company system, it is the Commission-jurisdictional intra-system agreement (not a state's decision as to recovery of retail stranded costs) that determines the allocation of costs at wholesale among the affiliates. Several of these commenters suggest that if the holding company believes that, as a result of a state's disallowance of costs in retail rate base, the cost allocations under an intra-system agreement are unduly discriminatory, the holding company could propose to amend the agreement.[757]

A number of commenters also express concern that services that investor-owned utilities provide to promote energy efficiency and conservation and to assist low-income residents and the elderly be continued.[758] NW Conservation Act Coalition suggests that the Commission should condition stranded cost recovery upon a showing by the utility that allowing recovery will not strand such social benefits.[759]

---

[756] *E.g.*, NARUC, Entergy Retail Regulators, MS Com, Al Com.

[757] *E.g.*, NARUC, MS Com.

[758] *E.g.*, Homelessness Alliance, Black Mayors, National Women's Caucus, Vann, La Raza.

[759] NARUC and OH Com assert that, in determining whether a wholesale transmission transaction is a "sham," the Commission should consider a retail customer's intent to bypass responsibility for supporting social programs.

Various commenters endorse the use by state regulators of a distribution charge or other fee imposed on electricity consumption to address stranded social benefits.[760] NARUC and OH Com express concern that the Commission, by claiming authority over unbundled retail transmission services, may make it difficult for states to use non-bypassable "wires charges" or "access fees" to require all customer classes to support such program.[761] NARUC asks the Commission to ensure that any jurisdiction we exercise over unbundled transmission services does not legally or practically foreclose the ability of individual states to fund such programs.[762] LILCO, as part of its argument that the Commission should provide a complete backstop for stranded cost recovery resulting from retail wheeling, urges the

---

[760] *E.g.*, Natural Resources Defense, NW Conservation Act Coalition, Seattle, FTC, Northeast States for Coordinated Air Use Management, NARUC, OH Com, CO Com agrees that states should have the option to fund such programs through the imposition of surcharges on any form of electric service used to benefit retail customers, including surcharges on retail transmission rates. Seattle proposes either a simple fee on kWhs or a differential fee based on the type of resource and its environmental affects. DOE urges the Commission to work with state regulators to ensure that states have the ability to recover stranded retail costs and benefits in a way that prevents cost-shifting, forum-shopping, and uneconomic bypass (including bypass of stranded benefits).

[761] CO Com notes that the NOPR proposes to limit states to funding mechanisms that can be implemented solely at the local distribution level, presumably through the use of a surcharge on distribution facilities or so-called "fee at the meter" or the use of a local distribution system revenue decoupling mechanism. It suggests that neither of these options may be legally or practically feasible in many states for a wide variety of reasons (but does not expand on these reasons).

[762] Natural Resources Defense proposes that the Commission adopt the following language: "The FPA does not affect state regulators' jurisdiction to apply distribution charges—either volume-based or fixed—to electricity that is used by any utility customer to provide end-use services (as distinguished from electricity that is purchased for resale to end-use customers). Natural Resources Defense Initial Comments at p. 3.

Commission to establish retail wheeling rates that provide for full recovery of any stranded costs. including stranded social benefits, that are unrecovered after state stranded cost determinations.

Commission Conclusion

We believe that both this Commission and the States have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in order to reach a different generation supplier, and that utilities are entitled, from both a legal and a policy perspective, to an opportunity to recover all of their prudently incurred costs. This Commission's authority to address retail stranded costs is based on our jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce. The authority of state commissions to address retail stranded costs is based on their jurisdiction over local distribution facilities and the service of delivering electric energy to end users. However, because it is a state decision to permit or require the retail wheeling that causes retail stranded costs to occur, we will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority[763] does not have authority under state law to address stranded costs when the retail wheeling is required.

Commenters that describe our action as an unlawful abdication or delegation of authority misconstrue the nature of our decision to leave retail stranded costs (with a limited exception) to state

[763] "State regulatory authority" has the same meaning as provided in section 3(21) of the FPA.

regulatory authorities.[764] We have not "abdicated" or "delegated" to state regulatory authorities our jurisdiction over the rates, terms, and conditions of retail transmission in interstate commerce; if retail transmission in interstate commerce by a public utility occurs, public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205. Instead, we have made a policy determination that the recovery of retail stranded costs—an issue over which either this Commission or state commissions could exercise authority by virtue of their jurisdiction over retail transmission in interstate commerce and over local distribution facilities and services, respectively—is primarily a matter of local or state concern that should be left with the state commissions. However, if the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required, then we will entertain requests to recover such costs.[765]

[764] We reject the arguments of EEI and Coalition for Economic Competition that the Commission made findings in the initial stranded cost NOPR that "inexorably" lead to the conclusion that Commission action providing full recovery of retail stranded costs is required. Their reliance on *Williams Natural Gas Company v. FERC*, 872 F.2d 438 (D.C. Cir. 1989), appeal after remand, 943 F.2d 1320 (D.C. Cir. 1991) (Williams), is simply misplaced. Williams involved a rulemaking that was terminated by the Commission. The court stated that the Commission, "having expressed these tentative views (that the incentive price for tight formation gas would disserve the public interest) and having solicited comments on the issue, was not free to terminate the rulemaking" without providing a satisfactory explanation. 872 F.2d at p. 446, 450. Here, in contrast, we are issuing a Final Rule that reaffirms in many aspects preliminary findings proposed in both the initial and Supplemental Stranded Cost NOPRs. Although the conclusion we reach based on those findings may be different than that which some commenters advocate, we have fully explained the basis for our decision.

[765] In these circumstances, the cases cited by commenters to support the proposition that an agency is not authorized to abdicate its statutory responsibilities or to delegate to parties and intervenors regulatory responsibilities (such as preparation of an environmental impact statement) are factual distinguishable and inapposite. *See, e.g.*, FPC v. Texaco, 417

Because we have accepted the view that stranded costs caused by retail wheeling are primarily a matter of local or state concern, we will not allow the states to use the interstate transmission grid as a vehicle for passing through any retail stranded costs, with the following limited exception. If the state regulatory authority does not have authority under state law when the retail wheeling is required to resolve the retail stranded cost issue, we will permit a utility to seek a customer-specific surcharge to be added to an unbundled transmission rate.

We believe that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling.[766] In addition, as further discussed in Section IV.I we are defining in this rule "facilities used in local distribution" under section 201(b)(1) of the FPA. Rates for services using such facilities to make a retail sale are state-jurisdictional, and states will be free to impose stranded costs caused by retail wheeling on facilities or services used in local distribution. States may also use their jurisdiction over local distribution facilities or services to recover so-called stranded benefits, This, rule is not intended to preempt any existing state authority to assess a stranded cost or stranded benefits charge on a retail customer that obtains retail wheeling. Moreover, since the charge is state jurisdictional, it is of no

U.S. 380, 394 (1974) (Commission cannot exempt small-producter rates from compliance with just and reasonable standard): *United States v. City of Detroit*, 720 F.2d 443, 451 (6th Cir. 1983) (district court inappropriately implied waiver of EPA statutory duty under Title 11 of the Federal Water Pollution Prevention and Control Act): *State of Idaho v. ICC*, 35 F.3d 585, 595-96 (D.C. Cir. 1994) (an agency cannot abdicate its NEPA responsibilities in favor of the regulated party).

[766] As discussed in the Supplemental NOPR (FERC *Statutes and Regulations* ¶32,514 at p. 33,129-30), these mechanisms include requiring an exit fee before a franchise customer is permitted to obtain unbundled retail wheeling and imposing a surcharge on local distribution rates. Commenters identified several other possible mechanisms in response to the initial Stranded Cost NOPR.

moment to our responsibilities under the FPA as to whether such charges are volume-based (kWh), demand-based kW), or customer based (fixed).

We believe that our approach to retail wheeling stranded costs represents an appropriate balance between federal and state interests. This approach ensures, that the rates for transmission in interstate commerce by public utilities (except in a narrow circumstance) will not be burdened by retail costs. It also helps to ensure that one State will not be able to impose costs stranded by its ordering of retail wheeling[767] on customers in another state.[768] In a holding company or other multi-state situation, we recognize that denial of retail stranded cost recovery by a state regulatory authority could, through operation of the reserve equalization formula in a Commission-jurisdictional intra-system agreement, inappropriately shift the disallowed costs to affiliated operating companies in other states. The Commission is concerned about this potential for cost-shifting. We would not wish to see an intra-system agreement used as a means for one jurisdiction to shift to other jurisdictions retail stranded costs for which it would otherwise be responsible under that agreement. However, we will deal with such situations if they arise pursuant to public utility filings under section 205 or complaints under section 206. Thus, the need to amend a jurisdictional agreement to prevent retail stranded costs from being shifted to customers in other states will be addressed on a case-by-case basis. We encourage the affected state commissions in such situations to seek a mutually agreeable approach to this potential problem. If such a consensus solution resulted in a filing to modify a

[767] As we stated in the Supplemental NOPR, we do not address whether states have the lawful authority to order retail wheeling in interstate commerce. Id. at p. 33, 098 at n.228. In addition, we are neither endorsing nor discouraging retail wheeling.

[768] See id. at p. 33,098, 33,127-28.

jurisdictional agreement, we would accord such a proposal deference, particularly if other interested parties support the filing. In the event that the state commissions and other interested parties cannot reach consensus that would prevent cost shifting, the Commission would ultimately have to resolve the appropriate treatment of such stranded costs.

Should a situation arise in which a state regulatory authority concludes that it has no ability to address retail stranded costs, or the appropriate state courts ultimately determine that a state regulatory authority does not have authority to impose retail stranded costs, a utility may seek recovery here through its Commission-jurisdictional retail transmission rates of costs stranded as of the date of the customer's departure. Because all parties are put on notice by this Rule of the potential for recovery through Commission-jurisdictional retail transmission rates should state commission-authorized retail wheeling charges be invalidated, such recovery (if allowed) would not be retroactive ratemaking.[769]

8. Evidentiary Demonstration Necessary—Reasonable Expectation Standard

In the Supplemental Stranded Cost NOPR, the Commission made a preliminary determination that a public utility or transmitting utility seeking to recover stranded costs must demonstrate that it had a reasonable expectation of continuing to serve a customer. We indicated that the existence of a notice of termination provision in a wholesale requirements contract creates a rebuttable presumption that the utility had no reasonable expectation of serving the customer beyond the period

[769] *See Public Utilities Commission of the State of California v. FERC*, 988 F.2d 154, 163-66 (D.C. Cir. 1993).

provided for in the notice provision.[770] We proposed not to adopt a mini-

* * * * *

Ohio Edison Company
Ohio Valley Electric Corporation
Oklahoma Gas & Electric Company
Old Dominion Electric Cooperative
Otter Tail Power Company
Pennsylvania Power Company
Peoples Electric Cooperative
Rayburn Country Electric Cooperative
Rochester Gas & Electric Corporation
Sierra Pacific Power Company
South Beloit Water, Gas & Electric Company
St. Joseph Light & Power Company
Superior Water Light and Power Company
Texas-New Mexico Power Company
Toledo Edison Company
Tucson Electric Power Company
UGI Utilities. Inc.
Union Electric Company
Union Light, Heat, & Power Company
Union Power Corporation
Upper Penninsula Power Company
Vermont Electric Transmission Company
Vermont Electric Power Company
Virginia Electric & Power Company
Yadkin, Inc.

[770] *FERC Statutes and Regulations* ¶32,514 at p. 33,117.

Appendix G

I. Legal Analysis of Commission Jurisdiction Over the Rates, Terms and Conditions of Unbundled Retail Transmission in Interstate Commerce

Based on an analysis of the relevant legislative history and case law under the Federal Power Act (FPA), the Commission concludes that it has exclusive jurisdiction over the rates, terms and conditions of the unbundled transmission in interstate commerce, by a public utility, of electric energy to an end user. This is also known as retail wheeling in interstate commerce.[1]

The Commission's jurisdiction over the rates, terms and conditions of transmission in interstate commerce derives from Congress' power to regulate interstate commerce under the United States Constitution[2] and the FPA. When Congress enacted the FPA, it gave the Commission exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. The Supremacy Clause of the Constitution provides that federal laws enacted pursuant to the powers delegated to the federal government by the United States Constitution are the supreme law of the land.[3] Accordingly, to the extent that retail wheeling involves transmission in interstate commerce by public utilities, the rates, terms and conditions of

[1] Section 212(h) of the FPA provides tat no order issued under the FPA shall be conditioned upon or require the transmission of electric energy directly to an ultimate consumer. 16 U.S.C. § 824k(h). The Commission's assertion of jurisdiction in this final rule is over the rates, terms and conditions of retail transmission that occurs voluntarily or as a resu!! of a state retail access program.

[2] U.S. Const. Art I, Section 8, cl.3.

[3] U.S. Const. Art, VI.cl.2.

such service are subject to the exclusive jurisdiction of the Commission, and must be filed with the Commission.[4]

1. Relevant Federal Power Act Provisions

Section 20 1(b)(1) of the FPA provides:

The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce* * *. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction * * * over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

16 U.S.C. 824(b)(1) (emphasis added).
Thus, the statute on its face limits Commission jurisdiction over sales of energy to sales at wholesale, but does not limit jurisdiction over transmission to transmission used only for wholesale sales.

Sections 201(c) and (d) define the meaning of "the transmission of electric energy in interstate commerce" and "sale of electric energy at wholesale in interstate commerce." Section 201(c) provides:

For the purpose of this Part, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

[4] *See Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246, 251-52 (1951) (*Montana-Dakota*).

16 U.S.C. 824(c). Section 201(d) provides:

The term "sale of electric energy at wholesale" when used in this Part means a sale of electric energy to any person for resale.

16 U.S.C. 824(d).

Sections 205 and 206 of the FPA give the Commission jurisdiction over the rates, terms and conditions of transmission in interstate commerce, and sales at wholesale in interstate commerce, by public utilities. 16 U.S.C. 824d and 824e.

2. Legislative History and Case Law

Much of the legislative history, of the FPA indicates that Congress intended the Commission's jurisdiction to extend only to those matters which the Attleboro decision[5] held to be beyond the reach of the States. For instance, the report accompanying the Senate bill states that subsection (b) "leaves to the States the authority to fix local rates even in cases where the energy is brought in from another State."[6] In other words, states retain authority to regulate rates of electric energy to ultimate consumers. The Senate report also states:

The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in (Attleboro) to be beyond the reach of the States. Jurisdiction is

[5] *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927) (Attleboro). In Attleboro, the Supreme Court held that State regulation of the interstate sale of electricity was barred by the Commerce Clause because such regulation would impose a "direct burden" on interstate commerce.

[6] S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). See also H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935).

asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines and over the generating facilities which produce energy[7] for interstate transmission and sale.

S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935) (emphasis added). Thus, federal jurisdiction over transmission lines is not dependent on whether those lines are used to effect a sale, wholesale or otherwise.

The provisions of FPA section 201 reserving certain regulatory authority to the States have been interpreted narrowly.[8] The Supreme Court has stated:

In section 201(b), Congress did no more than leave standing whatever valid state laws then existed relating to the exportation of hydroelectric energy; by its plain terms, section 201(b) simply saves from preemption under Part II of the Federal Power Act such state authority as was otherwise "lawful."[9]

[7] The provisions of the Senate bill regarding federal jurisdiction over generating facilities were eliminated from the final version of the bill.

[8] Section 201(a) declares that Federal regulation of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, "such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States." 16 U.S.C. § 824(a), Section 201(b)(1) states that the provisions of Part II of the FPA apply to the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce but, except as specifically provided, "shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line." 16 U.S.C. § 824(b)(1).

[9] *New England Power Co. v. New Hampshire*, 455 U.S. 331, 341 (1982) (NEPCO).

The Court also stated:

Nothing in the legislative history or language of the statute evinces a congressional intent 'to alter the limits of state power otherwise imposed by the Commerce Clause.' * * * or to modify the earlier holding of this Court concerning the limits of state authority to restrain interstate trade.[10]

Unlike the narrow interpretations given to the FPA provisions reserving certain regulatory authority to the States,[11] the courts have construed transmission "in interstate commerce" broadly. The term does not turn on whether the contract path for a particular power or transmission sale crosses state lines, but rather follows the physical flow of electricity. Because of the highly integrated nature of the electric system, this results in most transmission of electric energy being "in interstate commerce."

One of the earliest cases construing Commission jurisdiction over transmission was Jersey Central Power & Light Co. v. FPC, 319 U.S. 61 (1943) (Jersey Central). In that case, the Commission asserted jurisdiction over a New Jersey utility by showing that the utility owned transmission facilities that were used to transmit energy in interstate commerce. The Court found that the Commission had demonstrated that the utility owned transmission facilities that were indirectly interconnected, through a second New Jersey utility, to facilities owned by a

---

[10] *Id.* (citation omitted).

[11] While Congress may exercise its Commerce Clause authority to grant the States that "ability to restrict the flow of interstate commerce that they would not otherwise enjoy," Lewis v. BT Investment Managers, Inc., 447 U.S. 27, 44 (1980). States may not exercise such regulatory powers unless Congress has expressly stated its intention to take such an affirmative grant of power. *NEPCO*, 455 U.S. at p. 343.

New York utility and that the facilities were used to transmit electric energy in interstate commerce.

The Court noted that section 201(c) of the FPA defines electric energy "transmitted in interstate commerce to be energy transmitted from a State and consumed at any point outside thereof." The Court stated:

It is impossible for us to conclude that this definition (of transmission in interstate commerce) means less than it says and applies only to the energy at the instant it crosses the state line and so only to the facilities which cross the line and only to the company which owns the facilities that cross the line.

319 U.S. at 71. Thus, a critical question regarding the jurisdictional status of a wheeling transaction is whether the facilities used to provide the service transmit electric energy in interstate commerce.

In Connecticut Light & Power Co. v. FPC. 324 U.S. 515 (1945) (CL&P), the Court reviewed the Commission's finding that a Connecticut utility was jurisdictional because it owned transmission facilities that were used in interstate commerce. The Court generally embraced the Jersey Central standard for determining whether facilities are used to transmit electric energy in interstate commerce. The Court emphasized that whether certain facilities transmit electric energy in interstate commerce is more a technical than a legal question. The Court stated:

Federal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test.

324 U.S. at 529. Thus, the Court adopted the Jersey Central test providing that the Commission's jurisdiction generally extends

to transmission facilities that transmit electric energy in interstate commerce.

The Court also applied the Jersey Central test in FPC v. Florida Power & Light Co., 404 U.S. 453 (1972), affirming the Commission's finding of jurisdiction over a Florida utility. The Commission demonstrated that the utility transmitted power to another Florida utility's "bus"[12] and that power was simultaneously transferred from the "bus" to a Georgia utility. The Court upheld the Commission's finding that electric energy from the two Florida utilities was commingled and was therefore transmitted in interstate commerce, 404 U.S. at 463.

In all of the above cases, the Court's decisions turned on whether energy being transmitted flowed in interstate commerce as a technical matter. The decisions did not turn on whether the transmission of energy flowing in interstate commerce involved energy that was being sold for resale or was being sold to an end user. Thus, there is nothing in the statute, its legislative history, or the case law to indicate that the Commission's jurisdiction over rates, terms and conditions of transmission in interstate commerce extends only to wholesale transmission and not retail transmission. Indeed, the statute on its face gives the Commission jurisdiction over transmission in interstate commerce and makes no distinction between wholesale transmission and retail transmission.

However, there are two important limitations on Commission authority. First, as discussed above, the FPA does not give the Commission jurisdiction over sales of electric energy at retail. Such sales historically have been bundled sales (i.e. generation

[12] A bus is an electrical conductor which serves as a common connection for two or more electrical circuits. Electric Utility Rate Design Study, Glossary: Electric Utility and Ratemaking Load & Management Terms, Edison Electric Institute (Sept. 11, 1978).

and transmission), and courts and the Commission have recognized State jurisdiction over bundled sales of energy. Second, under section 201(b)(1) of the FPA, the Commission does not have jurisdiction over facilities used in local distribution. In CL&P, the Court stated that local distribution facilities are exempt from Commission jurisdiction even if those facilities "carry no energy except extra-state energy." 324 U.S. at 531.

In the next section the Commission further discusses the statutory provisions and case law that shed light on the demarcation between transmission and local distribution, and thus on the jurisdictional line between federal and State authority

II. Legal Analysis of Commission Jurisdictional Transmission Facilities and State Jurisdictional Local Distribution Facilities

Two specific circumstances are addressed:

First, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public Utility of electric energy from a third-party supplier to a purchaser who will then resell the energy to an end user?

Second, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to an end user?

Based on an analysis of the relevant legislative history and case law under the FPA, the Commission reaches the following conclusions. With respect to the first circumstance, the Commission concludes that a public utility's facilities used to deliver electric energy to a wholesale purchaser whether labeled

"transmission," distribution," or "local distribution" are subject to the Commission's exclusive jurisdiction under sections 205 and 206 of the FPA, and that a public utility's facilities used to deliver electric energy from the wholesale purchaser to the ultimate consumer are "local distribution" facilities subject to the rate jurisdiction of the state.[13]

With respect to the second circumstance, the Commission believes that, based on the particular facts of the case, some of the public utility's facilities used to deliver electric energy to an end-user may be FERC-jurisdictional transmission facilities, while some of the facilities used may be state-jurisdictional local distribution facilities.

We set forth below the relevant legislative history and cast law, our legal conclusion and the factors which we believe are indicative of whether facilities are used in "local distribution" or "transmission in interstate commerce," as those terms are used in the FPA.

1. Relevant Federal Power Act Provisions

The Commission's jurisdiction is set forth in section 201 of the FPA.[14] Section 201(b)(1) provides in pertinent part:

The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric

---

[13] There are, of course, facilities that are used to provide delivery to both wholesale purchasers and end users. In those situations, we believe that the Commission and the States have jurisdiction to set rates for the services that are within their respective jurisdictions. That facilities are used to serve resale and retail customers does not, however, necessarily mean that the facilities are local distribution facilities.

[14] 16 U.S.C. § 8224.

energy at wholesale in interstate commerce * * *. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction* * *over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.[15]

Some of the court decisions that construe jurisdictional facilities under section 201 also construe the Commission's jurisdiction under section 203. Section 203(a) provides, in relevant part:

No public utility shall sell, lease, or otherwise dispose of the whole of its facilities subject to the jurisdiction of the Commission* * *or by any means whatsoever, directly or indirectly, merge or consolidate such facilities or any part thereof with those of any other person* * *without first having secured an order of the Commission to do so.[16]

In addition, section 206(d) concerns facilities "under the jurisdiction of the Commission":

The Commission upon its own notion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the

---

[15] 16 U.S.C. § 824e(b) (emphasis added).

[16] 16 U.S.C. §824(b) (emphasis added).

Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.[17]

2. Legislative History of the FPA

The relevant legislative history of the general purposes of Title II of the FPA, and of section 201 in particular, focuses primarily on bundled sales of electric energy and does not directly address the issue of what constitutes local distribution as opposed to transmission in interstate commerce.

In discussing the general purposes of Title II of the House bill, the House Report states:

Title II* * *establishes for the first time regulation of electric utility companies transmitting energy in interstate commerce.

* * * * *

* * *Under the decision of the Supreme Court of the United States in (Attleboro), the rates charged in interstate wholesale transactions may not be regulated by the States. Part II gives the Federal Power Commission jurisdiction to regulate these rates. A "wholesale" transaction is defined to mean the sale of electric energy for resale and the Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce.[18]

In its analysis of section 201, the House Report states:

---

[17] 16 U.S.C. §824e(d) (emphasis added).

[18] H.R. Rep. No. 1318, 74th Cong., 1st Sess. 7-8 (1935).

As in the Senate bill no jurisdiction is given over local distribution of electric energy, and the authority of States to fix local rates is not disturbed even in those cases where the energy is brought in from another State.[19]

The Senate Report's discussion of the general purposes of the FPA states:

The decision of the Supreme Court in (Attleboro) placed the interstate wholesale transactions of the electric utilities entirely beyond the reach of the States. Other features of this interstate utility business are equally immune from State control either legally or practically.[20]

In discussing material differences between the final version of the Senate bill and the original version, the Senate Report states:

Subsection (b), formerly (a), which states the subject matter to which the part relates, has been clarified to make plain that it includes interstate transmission where there is no sale and excludes all facilities used only for production of transmission in intrastate commerce or in local distribution.[21]

In discussing section 201 of the Senate bill, the Senate Report further states:

---

[19] *Id.* at p. 27.

[20] S. Rep. No. 621, 74th Cong., 1st Sess. at p. 17 (1935). See id. at p. 18 ("The revision between the original and final versions of the Senate bill) has also removed every encroachment upon the authority of the States. The revised bill would impose Federal regulation only over those matters which cannot effectively be controlled by the States.")

[21] *Id.* at p. 19.

The rate-making powers a(the Commission are confined to those wholesale transactions which the Supreme Court held in (Attleboro) to be beyond the reach of the States. Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines and over the generating facilities which produce energy for interstate transmission and sale. It is obvious that no steps can be taken to secure the planned coordination of this industry on a regional scale unless all of the facilities, other than those used solely for retail distribution, are made subject to the jurisdiction of the Commission. Facilities used only for intrastate commerce or local distribution are expressly excluded from the operation of the act.[22]

The Conference Report adds little description regarding jurisdictional facilities. In reference to section 201(b) it states that:

[T]he language of the House amendment has been followed with a clarifying phrase added to remove any doubt as to the Commission's jurisdiction over facilities used for the generation and local distribution of electric energy to the extent provided in other sections of this part and the part next following.[23]

In addition to the above statements pertaining to section 201 of the FPA, Congress referenced distribution of energy in the legislative history of section 206(d). Section 206(d) was originally enacted as section 206(b) of the FPA. Under the

[22] *Id.* at p. 48. The provisions of the Senate bill regarding federal jurisdiction over generating facilities were eliminated from the final version of the bill.

[23] H.R. Conf. Rep. No. 1903, 74th Cong., 1st Sess. 74 (1935).

Regulatory Fairness Act of 1988,[24] section 206(b) was redesignated as section 206(d).

The Conference Report on the original FPA does not address section 206(b). The Senate Report on the FPA bill states in pertinent part:

Subsection (b) authorizes the Commission to investigate and determine the cost of the production or transmission to electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.* * * Since the ratemaking powers granted to the Commission apply only to the wholesale rates of energy sold in interstate commerce, this last subsection should be of great benefit in removing the practical difficulty which the States may encounter in regulating the interstate distribution rates which are left under their control. Such rate regulation involves the examination and valuation of property outside the State. The task is one requiring an agency with a jurisdiction broader than that of a single State. The authority of the Federal Commission is to render assistance to the State commissions in a way which would preserve and make more effective the jurisdiction which is thus left to the States.[25]

The House Report discusses section 206(b) as follows:

This subsection reaches those situations where electric energy is transmitted in interstate commerce by the same company

[24] Pub. L. No. 100-473, 102 Stat. 2299 (1988).

[25] S. Rep. No. 621, 74th Cong., 1st Sess. 51 (1935) (emphasis added).

which distributes it locally, and will greatly aid State commissions in fixing reasonable rates in such cases.[26]

Thus, the discussions in the two reports do not appear to contemplate a situation in which the transmitter and seller of electric energy are different, and neither is a "local" distributor. The House Report expressly refers to the same company being the transmitter and seller of electric energy. The Senate Report by its terms addresses the regulation of interstate distribution rates.[27]

The above legislative history on sections 201 and 206(b) does not provide any definitive answers to the questions raised. We therefore turn to the case law under the FPA.

3. Case Law Under the FPA

Jersey Central was the first of the major FPC jurisdictional cases considered by the Supreme Court. The case involved the acquisition by New Jersey Power and Light Company (New Jersey Power) of certain securities of Jersey Central Power & Light Company (Jersey Central), without the Commission's prior approval. The question before the Court was whether Jersey Central was a "public utility" under section 201(e)[28] of the FPA

---

[26] H.R. Rep. No. 1318, 74th Cong. 1st Sess. 29 (1935) (emphasis added).

[27] The Senate Report states that interstate distribution rates are left in the States' control. Obviously, the Senate drew a distinction between interstate distribution (left in the States' control) and interstate transmission (given to the FPC). Compare S. Rep. No. 621 at p. 49 with H.R. Rep. No. 1318 at p. 51.

[28] Section 201(e) defines a "public utility" as "any person who owns or operates facilities subject to such jurisdiction under this Part (other than facilities subject to such jurisdiction solely by reason of section 210, 211, or 212)." 16 U.S.C. § 824(e). The section adopted in 1935 did not contain the

so that the Commission's prior approval of the stock acquisition was necessary under section 203 of the FPA.

Jersey Central owned transmission facilities that connected to facilities that Public Service Electric & Gas Company (Public Service) owned. The interconnection of these transmission facilities was in New Jersey. Public Service's facilities in turn connected to the facilities of the Staten Island Edison Corporation (Staten Island Edison), a New York utility, at the mid-channel of Kill van Kull, a body of water separating New Jersey and New York. Jersey Central delivered energy to and received energy from Public Service under contract, and Public Service delivered energy to and received energy from Staten Island Edison under contract.[29]

The Court found that, although Jersey Central generated and received electricity only in New Jersey, some of the electric energy that it dispatched to Public Service "was instantaneously transmitted to New York."[30] The Court held that "[t]his evidence * * *furnishes substantial basis for the conclusion of the Commission that facilities of Jersey Central are utilized for the transmission of electric energy across state lines."[31] Therefore, the Court found that Jersey Central was a public utility within the meaning of section 201(e).[32]

---

parenthetical, which was adopted in 1978 as part of the Public Utility Regulatory Policies Act.

[29] Jersey Central, 319 U.S. at pp. 63-65.

[30] *Id.* at p. 66.

[31] *Id.* at p. 67 (citation omitted).

[32] *Id.* at p. 73.

The Court cited Attleboro, in which the Court found that the sale of locally produced electric energy for use in another state resulted in the transmission of electric energy in interstate commerce, even though title passed at the state line.[33] In Jersey Central, the Court explained the rationale for federal jurisdiction as follows:

(Section 201(c) of the FPA) defines the electric energy in commerce as that "transmitted from a State and consumed at any point outside thereof." There was no change in this definition in the various drafts of the bill. The definition was used to "lend precision to the scope of the bill." It is impossible for us to conclude that this definition means less than it says * * *. The purpose of this act was primarily to regulate the rates and charges of the interstate energy. [34]

The Court in Jersey Central thus interpreted the FPA as placing within the federal province regulation of wholesale sales of electric energy that, in any manner, flows in interstate commerce. The language quoted above and the citation to section 201(c) of the FPA, to be relied upon in subsequent Supreme Court cases, strongly suggested that the Commission's jurisdiction was not based on whether there was a sale by the utility, but rather on the flow of electric energy either into or out of a state, so long as the energy crosses state lines.

CL&P, which was decided two years after Jersey Central, is the leading case interpreting the section 201(b) local distribution proviso. In CL&P, the Commission sought to regulate the accounting practices of Connecticut Light & Power Company

---

[33] 273 U.S. at pp. 86, 89-90.

[34] 319 U.S. at p. 71 (footnote omitted).

(CL&P).[35] At issue was whether CL&P was a "public utility," under the FPA. The utility's system encompassed an area solely within a single state (Connecticut)[36] and did not interconnect with any other company that operated out of state.[37] "Its purchases and sales, its receipts and deliveries of power, (were) all within the state."[38] However, CL&P did purchase energy from companies that had, in turn, purchased energy from Massachusetts. The company also sold energy to a municipality that exported a portion of that energy to fishers Island, located off the coast of Connecticut but "territory of New York."[39] The Commission based its jurisdiction on these few transactions.[40]

The Court of Appeals affirmed the Commission, holding that the Commission's jurisdiction extended to "electric distribution systems which normally would operate as interstate businesses." The Court of Appeals found that:

Whether or not the facilities by which petitioner distributes energy from Massachusetts should be classified as 'local' is not relevant to this case. The sole test of jurisdiction of the Commission over accounts is whether these facilities, 'local' or

---

[35] CL&P, 324 U.S. at p. 517.

[36] *Id.* at p. 518.

[37] *Id.* at p. 521.

[38] *Id.* at p. 522.

[39] *Id.* at pp. 519-21.

[40] *Id.*

otherwise, are used for the transmission of electric energy from a point in one state to a point in another.([41])

The Supreme Court reversed. It held that the statutory language in Section 201(b) of the FPA providing that the Commission "shall not have jurisdiction * ** over facilities used in local distribution" is a limitation upon Commission jurisdiction that "the Commission must observe and the courts must enforce."[42] In analyzing the statute, the Court stated:

It has never been questioned that technologically generation, transmission, distribution and consumption are so fused and interdependent that the whole enterprise is within the reach of the commerce power of Congress, either on the basis that it is, or that it affects, interstate commerce if at any point it crosses a state line.

* * * * *

But whatever reason or combination of reasons led Congress to put the provision in the Act, we think it meant what it said by the words "but shall not have jurisdiction* * *over facilities used in local distribution." Congress by these terms plainly was trying to reconcile the Claims of federal and local authorities and to apportion federal and state jurisdiction over the industry.[43]

---

[41] *Id.* at p. 522, *quoting Connecticut Light & Power Co. v. FPC*, 141 F.2d 14, 18 (D.C. Cir. 1944).

[42] 324 U.S. at p. 529.

[43] *Id.* at pp. 529-31.

The Court decided that this limitation on jurisdiction was "a legal standard that must be given effect in this case in addition to the technological transmission test."[44]

The Court stated that whether or not local distribution facilities carried out-of-state electric energy was irrelevant. Whatever the origin of the electric energy they carried, so long as the utility used the lines for local distribution,[45] they were exempt from federal jurisdiction.[46] In fact, the Court stated that local distribution facilities "may carry no energy except extra-state energy and still be exempt under the Act." Id. at 531. The Court concluded that the Commission's order:

Must stand or fall on whether this company owned facilities that were used in transmission of interstate power and which were not facilities used in local distribution.[47]

Upon reversing the Court of Appeals, the Court commented, in dictum, on the evidence the Commission had relied upon in finding that the facilities in question were used for transmission. It noted that the Commission had relied upon certain gas transportation cases in concluding that transmission extends from the generator to the point where the function of conveyance in bulk over distance is completed and the process of subdividing the energy to serve ultimate consumers, which is the characteristic of "local distribution," is begun. The Court cautioned:

---

[44] *Id.* at p. 531.

[45] It appears that while the Company received power (at one location) at 66 kV, it primarily owned facilities at 13.8 kV and below.

[46] 324 U.S. at p. 531.

[47] *Id.* at p. 531 (emphasis added).

But a holding that distributing gas at low pressure to consumers is a local business is not a holding that the process of reducing it from high to low pressure is not also part of such local business. In so far as the Commission found in these cases a rule of law which excluded from the business of local distribution the products of reducing energy from high to low voltage in subdividing it to serve ultimate consumers, the Commission has misread the decisions of this Court. No such rule of law has been laid down.[48]

The Court also noted in its dictum, however, that once a company is properly found to be a "public utility" under the Act, the fact that a local commission may also have jurisdiction does not preclude exercise of the Commission's functions. Id. at 533.[49] The Court instructed the lower court to remand the case to the Commission for a finding regarding whether the facilities in question were used in local distribution.[50]

---

[48] *Id.* at p. 534.

[49] *See United Stats v. Public Utilities Commission of California*, 345 U.S. 295, 316 (1953) (Public Utilities Commission): Certainly the concrete fact of resale of some portion of the electricity transmitted from a state to a point outside thereof invokes federal jurisdiction at the outset, despite the fact that the power thus used traveled along its interstate route "commingled" with other power sold by the same seller and eventually directly consumed by the same purchaser-distributor.

See also Arkansas Power & Light Co. v. FPC, 368 F.2d 376, 383 (8th Cir. 1966) ("Where a company is in fact a public utility , all wholesale sales for resale in interstate commerce are subject to the provisions of sections 205 and 206 of the (FPA), regardless of the facilities used."). The Eighth Circuit further noted that the section 201(b) exemption applies to a company's status as a public utility and not to the Commission's jurisdiction over sales in interstate commerce for resale. *Id., citing Public Utilities Commission, Colton, infra. and Wisconsin-Michigan, infra.*

[50] *Id.* at p. 536.

The CL&P case was ultimately disposed of without the Commission having made a finding that the facilities were used in local distribution. While the Commission found that it was "extremely doubtful" that it could find that the facilities in question were not local distribution facilities, 6 FPC 104, 106 (1947), the Commission did not articulate a definition of local distribution facilities.

In Wisconsin-Michigan Power Co. v. Federal Power Commission,[51] the Seventh Circuit held that a utility was a jurisdictional public utility where it operated two divisions in Wisconsin and Michigan in a coordinated manner such that electric energy from one state was transmitted to the other, and vice versa, "in appreciable amounts by the power company and by it commingled with energy generated in the two respective districts and then delivered to the [wholesale] customers* * *.[52] The court also rejected the notion that the energy changed its form or character when it was stepped down in voltage before it reached the wholesale purchasers.[53]

The court in Wisconsin-Michigan distinguished between transmission and local distribution by focusing on wholesale sales of electric energy versus retail sales ("local rates") of electric energy. It cited the House Report on the FPA, and characterized the legislative history as follows:

---

[51] 197 F.2d 472 (7th Cir. 1952), cert denied, 3345 U.S. 934 (1953) (*Wisconsin-Michigan).*

[52] *Id.* at p. 474.

[53] *Id.* ("Obviously the energy thus transmitted in interstate commerce is not changed in form or in character except that the voltage is reduced to an extent consistent with efficient economic management and operation").

The legislative history, (H.R. Rep. No. 1318). 74th Cong., 1st Sess. pages 7, 8 and 27 (1935), discloses that the Congressional Committee intended that the provisions of the (FPA) should apply to the transmission of electric energy in interstate commerce, i.e., the sale of energy at wholesale in interstate commerce, but not to the retail sale of any such energy in local distribution; that the (FPA) left to the state the authority to fix local rates where the energy is brought in from other states, and that the rate making power of the (FPC) was to be confined to those wholesale transmissions which the Supreme Court had held in (Attleboro) to be beyond the reach of the state. Under that decision, said the committee, the rates charged in interstate wholesale transactions could not be regulated by the states. It defined a wholesale transaction as the sale of electric energy for resale.[54]

The Seventh Circuit's characterization of the House Report seems to equate transmission of electric energy in interstate commerce with the sale of energy at wholesale in interstate commerce. However, this interpretation is at odds with both the plain words of the statute as well as the language of the House Report, both of which refer to transmission in interstate commerce separately from sales for resale in interstate commerce.[55] In addition, the Senate Report, which the Seventh Circuit did not mention, clearly recognized jurisdiction over all

[54] 197 F.2d at p. 476 (emphasis added).

[55] See H.R. Rep. No. 1318 at p. 27, ("Subsection (b) confers jurisdiction upon the Commission over the transmission of electric energy in interstate commerce and the sale of electric energy in wholesale in interstate commerce * * *." emphasis added.),

interstate transmission lines, whether or not a sale of energy is carried by those lines.[56]

The Wisconsin-Michigan court also cited analogous natural gas cases, stating that "[t]he question is essentially, when does interstate commerce transportation end and where do the local distribution facilities first become operative."[57] The court further stated that:

(U)pon delivery to (the wholesaler) local distribution begins when he resells. His sales and distribution at retail are clearly local in character, and constitute only local distribution: but at no point before delivery to him has been completed, has interstate transmission terminated. In other words, "facilities used in local distribution" means facilities used for making resale and distribution to consumers, jurisdiction over which is left to the states. It was only because of this conclusion that the Supreme Court said, (citation omitted), the Act "cut(s) sharply and cleanly between sales for resale and direct sales for consumptive uses." We think there is no ground for the position that local distribution includes any transmission occurring before the wholesaler who resells at retail is reached.[58]

The Seventh Circuit concluded that the sales for resale were made in interstate commerce; that local distribution had not begun; that the interstate character of the transmission persisted until delivery to the wholesaler; that, up to that point, no local

[56] See S. Rep. No. 621 at p. 48 ("Jurisdiction is asserted over all interstate transmission line whether or not there is a sale of electric energy carried by those lines* * *.).

[57] 197 F.2d at p. 477.

[58] *Id. citing FPC v. East Ohio Gas Co.*, 338 U.S. 464 (1950) (East Ohio).

distribution facilities were in operation and that, therefore, the sales were subject to Commission regulation.

In Federal Power Commission v. Southern California Edison Company (the Colton case),[59] the Supreme Court held that the FPA provides a clear line of demarcation between jurisdictional transactions and non-jurisdictional transactions. However, this case, too involved bundled sales of electric energy. In the facts of the case, Southern California Edison Company (Edison) admitted that it was a public utility by virtue of owning two interstate transmission lines.[60] At issue was whether its sales of electric energy to the City of Colton, California, for resale to Colton's retail customers, were jurisdictional. Included in the electric energy that Edison sold to Colton was out-of-state electric energy from Hoover Dam.[61] The Commission ruled that the sale to Colton was a sale of electric energy at wholesale in interstate commerce subject to regulation under the FPA.[62] In upholding the Commission, the Court held that Edison's importation of out-of-state electricity for resale to Colton sufficed to confer federal jurisdiction.

---

[59] 376 U.S. 205 (1964) (Colton).

[60] The Supreme Court noted that Edison's status as a public utility did not decide the question of whether the FPC could assert jurisdiction over the rates for the Edison-Colton sale, Id. at p.208 n.3.

[61] *Id.* at p. 208, 209 & n.5.

[62] *Id.* app. 208, *See Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, 461 U.S. 375, 380 (1983))"(Colton) held, among other things, that * * *a California utility that received some its power from out-of-state was subject to federal and not state regulation in its sales of electricity to a California municipality that resold the bulk of the power to others.").

The Court. citing an earlier Supreme Court case,[63] characterized Congressional intent in the FPA:

(W)hat Congress did was to adopt the test developed in the Attleboro line which denied state power to regulate a sale "at wholesale to local distributing companies" and allowed state regulation of a sale at "local retail rates to ultimate consumers."[64]

The Court rejected the argument that FPC jurisdiction was confined to those inter-state wholesale sales constitutionally beyond the power of state regulation by force of the Commerce Clause, and was to be determined on a case-by-case analysis of the impact of state regulation upon the national interest. The Court stated that in the FPA:

(C)ongress meant to draw a bright-line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis. This was done in the Power Act by making FPC jurisdiction plenary and extend[ed] it to all wholesale sales in interstate commerce except those which Congress has made explicitly subject to regulation by the States.[65]

The Court held that "(t)here is no such exception covering the Edison-Colton sale."[66]

---

[63] *Illinois Natural Gas Co. v. Central Illinois Public Service Co.*, 314 U.S. 498, 504 (1942).

[64] 376 U.S. at p. 214.

[65] *Id.* at pp. 215-216.

[66] *Id.* at p. 216 (footnote omitted).

Parties in the Colton case had raised the question of whether jurisdiction over the Colton sale was prevented by the "local distribution" proviso of section 201 (b). The Court stated that whether facilities are local distribution facilities is a matter for the Commission to decide in the first instance. Citing CL&P, supra, it stated:

Whether facilities are used in local distribution although a limitation on FPC jurisdiction and a legal standard that must be given effect in addition to the technological transmission test* * * involves a question of fact to be decided by the FPC as an original matter.[67]

The Court cited evidentiary support and the Commission's expertise in such matters in upholding the Commission' determination that certain facilities owned by Edison were used exclusively to effect the wholesale sale to Colton and not for local distribution. Such facilities included 12 kV lines that served an industrial customer, several lighted highway signs, a residence and a railroad section house before they reached the transformers in the Colton substation. The FPC had held that those uses prior to the line reaching the Colton substation did no transform the lines into local distribution facilities.[68]

In Duke Power Company v. Federal Power Commission (Duke),[69] the D.C Circuit held that a public utility's acquisition of facilities used solely in local distribution, and which would continue to be used for local distribution, was beyond the Commission's jurisdiction under section 203. The case involved

[67] *Id.* at p. 210 n. 6 (citation omitted).

[68] *Id.* at p. 210 n.6.

[69] 401 F.2d 930 (D.C. Cir. 1968) (Duke).

Duke Power Company's (Duke's) proposed acquisition of facilities owned by Clemson University (Clemson), which were used to distribute electricity off-campus to customers (primarily university personnel) in two South Carolina counties. Clemson purchased the power at wholesale from Duke. No one appeared to contest the conclusion that the 7 miles of distribution line and 418 service connections owned by Clemson were "local distribution" facilities.[70] Rather, the case turned on interpreting section 203 and whether it was intended to affect only acquisitions of jurisdictional facilities, or also to affect acquisitions of non-jurisdictional facilities. In interpreting section 203, however, the D.C. Circuit extensively analyzed and discussed the fundamental jurisdictional lines that Congress drew in section 201.

Citing to the CL&P case, the court in Duke stated:

The Act, as we have seen, effectuated federal control over the transmission and the sale at wholesale of electric energy in interstate commerce, and established the Commission's regulatory power over public utilities engaging in either of these pursuits.[71]

However, quoting CL&P, the court further stated:

The expression "facilities used in local distribution" is one of relative generality. But as used in this Act it is not a meaningless generality in the light of our history and the structure of our government. We hold the phrase to be a limitation on jurisdiction

[70] Duke delivered power to Clemson at a distribution voltage of 4,160 volts. The step-down transformers by which the voltage was reduced, and the substations at which the delivery was effected, were owned by Duke, 401 F.2d at p. 931, n.8.

[71] 401 F.2d at pp.938-39 (emphasis added, footnotes omitted).

and a legal standard that must be given effect in this case in addition to the technological transmission test.[72]

The court further rejected the Commission's concept that, in order to determine whether jurisdiction over any particular acquisition existed, the impact of local supervision be measured on a case-by-case basis. Quoting from Colton, the court Stated:

[T]his "flexible approach"—involving as it does the consideration, inter alia, of "the effect of the regulation upon the national interest in the commerce"—has been flatly-rejected as a technique for resolving jurisdictional conflicts between the Commission and state bodies.* * * We think that like the line "(i)t cut sharply and cleanly between sales for resale and direct sales for consumptive uses" to facilitate jurisdictional determinations in rate regulation. "Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis." in distributing regulatory power over the acquisition of facilities.[73]

The court rejected the Commission's argument that jurisdiction over the merger or consolidation of jurisdictional facilities with those of any other "person" under section 203 gave the Commission jurisdiction over Duke's acquisition. The court stated that the FPA reflects a policy "' that matters largely of a local nature, even though interstate in character, should be handled locally and should receive the consideration of local (officials) familiar with the local conditions in the communities involved.[74]

---

[72] *Id.* (footnote omitted).

[73] *Id* at p. 949 (footnotes omitted).

[74] *Id.* at p. 936 (quoting from Hearings on H.R. 5432 before the House Committee on Interstate and Foreign Commerce, 74th Cong., 1st Sess. 393 (1935) (testimony of then-FPC Commissioner Seavey)).

Federal Power Commission v. Florida Power & Light Company[75] is the last major court case to address the Commission's transmission jurisdiction. In this case, the Commission sought to impose its accounting rules upon Florida Power & Light Company (Florida Power & Light). The company's system lay solely within the borders of Florida and did not directly connect with any out-of-state utility.[76] The Commission held that Florida Power & Light did own facilities that transmitted electric energy in interstate commerce, but the Court of Appeals for the Fifth Circuit ruled that the Commission did not have substantial evidence to support its finding.

The Supreme Court reversed. The Supreme Court noted that Florida Power & Light was a member of the Florida Power Pool along with Florida Power Corporation (Florida Power Corp.).[77] In turn, Florida Power Corp. connected with Georgia Power Company (Georgia Power) at a "bus"[78] south of the Georgia-Florida border.[79] Florida Power Corp. regularly exchanged power with Georgia Power.[80] In many instances, Florida Power Corp. transferred power to Florida Power & Light instantly after receiving power from Georgia Power, and transferred power to Georgia Power immediately after receiving

---

[75] 404 U.S. 453, *reh'g denied*,U.S. 948 (1972) (*Florida Power & Light).*

[76] 404 U.S. at p. 456.

[77] *Id.* at p. 456.

[78] A "bus" is a connector or group of connectors that serves as a common connection for two or more circuit.

[79] 404 U.S. at p. 457.

[80] *Id.*

power from Florida Power & Light.[81] The Supreme Court found that power commingled in the bus moved across state lines, and concluded that Florida Power & Light engaged in transmission in interstate commerce. The Court held that to establish jurisdiction, the Commission need only show that "some (Florida Power & Light) power goes out of State."[82] The Court further explained that "(i)f any (Florida Power & Light) power has reached Georgia, or (if Florida Power & Light) makes use of any Georgia power* * *FPC jurisdiction will attach* * *.[83]

There is also a line of cases that address, among other things, what constitutes a Commission jurisdictional "sale of electric energy at wholesale"[84] under section 201 of the FPA.[85] These cases all concerned bundled sales. While the issues posed above involve unbundled wheeling, the "resale cases are helpful to the extent they suggest that local distribution takes place only after power is subdivided. See, e.g., 345 U.S. at 316 ("the facilities supplied 'local distribution' only after the current was subdivided for individual consumers.").

---

[81] *Id.* at p. 457 & n.8.

[82] *Id.* at p. 461 (emphasis omitted).

[83] *Id.* at p. 461 n. 10, (emphasis added).

[84] See Section 201(d), 16 U.S.C. § 824(d) (1988).

[85] *Public Utilities Commission*, supra note 345: *City of Oakland, California v. FERC*, 754 F.2d 1378 (9th Cir. 1985) (*Oakland*). *See also Alexander v. FERC*, 609 F.@d 543 (D.C. Cir. 1979) (*Alexander*).

4. Natural Gas Act

The Natural Gas Act (NGA) was adopted in 1938. Like the FPA, the NGA contains language limiting the Commission's jurisdiction in situations involving local distribution.[86]

Section 1(b) of the NGA provides:

The provisions of this Act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.[87]

There is similarity in many respects between the House and Senate Reports on the FPA and the NGA with respect to the jurisdiction given the Commission. For example, all four reports mention Attleboro as placing interstate wholesale transactions beyond the reach of the States. As indicated in the House Report on the NGA, the States could "regulate sales consumers even though such sales are in interstate commerce, such sales being considered local in character and in the absence of congressional prohibition subject to State regulation." (See H.R. Rep. No. 709, 75th Cong., 1st Sess. 1). However, the House and Senate Reports on the NGA contain identical language not found in the reports on the FPA:

---

[86] Courts often rely on cases construing the NGA when interpreting the FPA, and vice versa, *E.g., Arkansas Louisiana Gas Co. v. Hall*, 4453 U.S. 571, 577 n.7 (1981).

[87] 15 U.S.C. § 717(b) (emphasis added).

In view of the importance of section 1(b), which states the scope of the act, it seems advisable to comment on certain provisions appearing therein. It will be noted that this subsection of the bill, after affirmatively stating the matters to which the act is to apply, contains a provision specifying what the act is not to apply to, as follows:

But shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

The quoted words are not actually necessary, as the matters specified therein could not be said fairly to be covered by the language affirmatively stating the jurisdiction of the Commission, but similar language was in previous bills, and, rather than invite the contention, however unfounded, that the elimination of the negative language would broaden the scope of the act, the committee has included it in this bill. That part of the negative declaration stating that the act shall not apply to "the local distribution of natural gas" is surplusage by reason of the fact that distribution is made only to consumers in connection with sales, and since no jurisdiction is given to the Commission to regulate sales to consumers the Commission would have no authority over distribution, whether or not local in character. (Emphasis added).[88]

As a result of this language it can be argued that Congress considered distribution (and local distribution) only in the context of bundled retail sales of natural gas. In fact, it appears that all of the court cases affirming the states' right to regulate local distribution of gas have involved bundled retail sales. See

[88] H.R. Rep. No. 709, 75th Cong., 1st Sess. 37 (1937): S. Rep. No. 1162, 75th Cong., 1st Sess. 3 (1937).

Panhandle Eastern Pipe Line Co. v. Michigan Public Service Commission, 341 U.S. 329 (1951) (Panhandle). There the Court, in affirming the State of Michigan's right to regulate an interstate pipeline's proposed bundled retail sales of gas to industrial consumers, noted that the pipeline company proposed to lay pipeline in "the streets and alleys of Detroit" and ignored the local distribution company's request for additional gas to meet the increased needs of the industrial consumers. Id. at 333. While the Court based its holding on a state's authority to regulate direct (retail) sales to an end-user, rather than on the basis of the section 1(b) local distribution provision, it also found that the proposed sales were "primarily of local interest" and "emphasized the need for local regulation." Id. Two years before Panhandle, the Supreme Court issued its decision in FPC v. East Ohio Gas Co., 338 U.S. 465 (1949) (East Ohio). East Ohio Gas Company owned and operated a natural gas business wholly within the State of Ohio. The company sold gas only to Ohio customers but most of the gas was transported to Ohio from other states by interstate pipelines. These interstate pipelines connected inside Ohio with East Ohio's large high pressure lines. The gas then was transported over 100 miles through East Ohio's system to its local distribution system. East Ohio argued that it was exempt from Commission jurisdiction because all of its facilities were local distribution.

The Court disagreed, finding the Commission's jurisdiction extends over the transportation of gas in interstate commerce through high-pressure transmission lines and that distribution did not begin until the point where pressure is reduced and gas enters local mains. The Court stated that: "[w]hat Congress must have meant by 'facilities' for 'local distribution' was equipment for distributing gas among customers within a particular local

community, not the high-pressure pipelines transporting the gas to the local mains."[89]

The Commission relied in part on East Ohio's high pressure/low pressure distinction in a recent NGA section 7 certificate case which authorized construction of facilities to bypass the local distribution company.[90] On appeal, the California Commission argued that under section 1(b) it should at least have "jurisdiction over the 'taps, meters and other tie-in facilities' that link the pipeline to end users."[91] The court disagreed:

While as a matter of ordinary English 'local distribution' might be understood to encompass any delivery to an end user, that is hardly the only or even more plausible reading. Distribution conjures up receiving a large quantity of some good and parcelling it out among many takers.[92]

After reviewing the report language discussed above, the court also stated:

Insofar as congressional committees spoke to the matter * * * they appear to have viewed distribution as confined to its

---

[89] 338 U.S. at pp 469-70.

[90] *See Mojave Pipeline Company*, 35 FERC ¶ 61,199 (1986), *reh'g denied*, 41 FERC ¶61,040 (1987), *reh'g denied*, 42 FERC ¶61,351 (1988): *see also Mojave Pipeline Company*, 66 FERC ¶61,194 (1994), *reh'g pending*.

[91] *See Public Utilities Commission of the State of California v. FERC, et al.*, 900 F.2d 269, 273 (D.C. Cir. 1990) (footnote omitted) (*WyCal*).

[92] *Id.* at p. 276.

parcelling out function and (probably) even more narrowly, to parcelling out accompanied by retail sales.[93]

In Cascade Natural Gas Corporation v. FERC, et al. (Cascade), the court affirmed the Commission's authorizing an interstate pipeline under section 7 of the NGA "to construct a tap and meter facility that would allow it to deliver natural gas directly to two industrial consumers* * *"[94] To reach the interstate pipeline, the industrials constructed a nine mile pipeline. Together, the facilities by-passed the local distribution company.[95]

The court rejected arguments that section 1(b) deprived the Commission of jurisdiction holding that:

"Local distribution." as Congress viewed the term, involves two components: the retail sale of natural gas and its local delivery, normally through a network of branch lines designed to supply local consumers.[96]

5. Analysis

a. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party

---

[93] *Id.* (emphasis in original).

[94] 955 F.2d 1412, 1414 (10th Cir. 1992).

[95] Unlike the situation in WyCal where the pipeline made direct sales to end users, in *Cascade*, the pipeline transported gas purchased from third parties. *See Northwest Pipeline Corporation*, 51 FERC ¶61,289 at p. 61,909 (1990).

[96] Cascade, 955 F.2d at p. 1421.

supplier to a purchaser who will then re-sell the energy to an end user?

The case law supports the conclusion that any facilities of a public utility used to deliver electric energy in interstate commerce to a wholesale purchaser, whether such facilities are labeled "transmission," "distribution" or "local distribution," are subject to the Commission's jurisdiction under sections 205 and 206.

This conclusion is supported by Public Utilities Commission, supra, in which the Supreme Court, in the section of its opinion addressing the section 201(b) local distribution provision, held that local distribution facilities began "only after the current was subdivided for individual consumers."[97] Wisconsin-Michigan. supra, in which the Seventh Circuit held that there is no local distribution until the wholesaler who re-sells at retail is reached, is to like effect.

This conclusion, which results in a "functional" line being drawn to determine Commission jurisdiction, is not only consistent with the case law under section 201, but is also consistent with our interpretation of the line drawn under newly amended FPA sections 211 and 212. As long as electric energy is being sold to a legitimate wholesale purchaser, we believe the Commission has jurisdiction under sections 201, 205, and 206 of the FPA over the public utility's facilities used to deliver electric energy to that purchaser.

b. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier directly to an end user?

---

[97] 345 U.S. at p. 316 (footnote omitted).

In analyzing jurisdiction over unbundled retail wheeling, we believe it is important to distinguish between unbundled wheeling provided by the public utility who previously provided bundled retail service to the end user, and unbundled wheeling provided by other public utilities to the end user. For example, a former bundled retail customer may need unbundled wheeling services from its previous public utility generation supplier, as well as unbundled wheeling from one or more intervening public utilities, in order to reach a distant generation supplier. In this scenario, the Commission believes it would have jurisdiction over all of the facilities used for the unbundled wheeling provided by the intervening public utilities.[98] The more difficult issue is whether some portion of the facilities used to transmit energy from the transmitting utility in closest proximity to the end user (the former supplier of the bundled product) is local distribution facilities. We believe that in most, if not all circumstances, some portion will be local distribution facilities.

The case law is replete with statements that the local distribution provision of section 201 must be given effect. However, the Supreme Court in both CL&P and Colton, supra, has stated that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. Thus, there is no clear case law on a "bright line" between transmission and local distribution. In addition, regardless of the details of the chain of delivery services necessary to move electric energy from the generator to the end user, in most cases the last public utility in the chain will use facilities that historically were considered local distribution facilities. Accordingly, unlike the situation involving unbundled wholesale wheeling, for which the case law clearly supports a "functional" test, the Commission believes the case law and

---

[98] The Commission would not have jurisdiction over the rates for the sale of generation by the distant supplier because the transaction would be a retail sale of electric energy.

practical realities of a changing industry support an analysis of local distribution facilities based on the facilities' functional as well as technical characteristics.

While it would be preferable to draw an absolutely "bright" line (e.g.. based on technical characteristics such as voltage), the Commission does not believe this is required by the case law and, importantly, would not be a workable approach in all cases because of the variety of circumstances that may arise and because utilities themselves classify facilities differently (e.g., one utility may classify a 69 kV facility as transmission; another may classify it as distribution).

Therefore, the Commission is adopting several indicators it will evaluate in determining whether particular facilities are transmission or local distribution in the case of vertically integrated transmission and distribution utilities:[99]

- Local distribution facilities are normally in close proximity to retail customers.

- Local distribution facilities are primarily radial in character.

- Power flows into local distribution systems, it rarely, if ever, flows out.

- When Power enters a local distribution system, it is not reconsigned or transported on to some other market.

- Power entering a local distribution system is consumed in a comparatively restricted geographical area.

---

[99] In the case of a distribution-only utility, which is franchised by a State of local government and sells only at retail, all of the circuits (and related wires, transformers, towers, and rights of way) which it owns or operates (regardless of voltage) would be local distribution facilities.

- Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

- Local distribution systems will be of reduced voltage.[100]

In summary for unbundled wholesale wheeling the Commission will apply a functional test. The only definitive question will be whether the entity to whom the power is delivered is a lawful wholesaler. For unbundled retail wheeling the Commission will apply a combination functional- technical test that will take into account technical characteristics of the facilities used for the wheeling. The Commission concludes that these tests are consistent with the FPA, its legislative history and the case law discussed above.

---

[100] The Commission has analyzed utilities' filings required by the Commission's regulations. These filings are made on FERC Form No. 1. While there is no uniform breakpoint between transmission and distribution, it appears that utilities account for facilities operated at greater than 30 kV as transmission and that distribution facilities are usually less than 40 kV.

APPENDIX E

Section 31,048 Federal Energy Regulatory Commission Regulations Preambles (Order 888-A)

[¶ 31,048]

62 F.R. 12274 (March 14, 1997)
18 C.F.R. Part 35
[Docket Nos. RM95-8-001 and RM94-7-002; Order No. 888-A)

Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities

(Issued March 4, 1997)

AGENCY: Federal Energy Regulatory Commission.

ACTION: Final rules; order on rehearing.

SUMMARY: The Federal Energy Regulatory Commission. (Commission) reaffirms its basic determinations in Order No. 888 and clarifies certain terms. Order No. 888 requires all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce to have on file open-access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service. Order No. 888 also permits public utilities and transmitting utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open-access and Federal Power Act section 211 transmission services. The Commission's goal is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers.

EFFECTIVE DATE: Changes to Order No. 888 made in this order on rehearing will become effective on [insert date 60 days after date of publication in the Federal Register].

FOR FURTHER INFORMATION CONTACT: David D. Withnell (Legal Information—Docket No. RM95-8-001), Office of the General Counsel, Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-2063.

Deborah B. Leahy (Legal Information—Docket No. RM94-7-002), Office of the General Counsel, Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.S. 20426, (202) 208-2039.

Dan T. Hedbert (Technical Information—Docket No. RM95-8-001), Office of Electric Power Regulation, Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-0243.

Joseph M. Power (Technical Information—Docket No. RM94-7-002), Office of Electric Power Regulation, Federal Energy Regulatory Commission, 888 First Street, N.E., Washing, D.C. 20426, (202) 208-1242.

SUPPLEMENTARY INFORMATION: In addition to publishing the full text of this document in the Federal Register, the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in the Public Reference Room at 888 First Street, N.E., Washington, D.C. 20426.

The Commission Issuance Posting System (CIPS), an electronic bulletin board service, provides access to the texts of formal documents issued by the Commission. CIPS is available at no charge to the user and may be accessed using a personal computer with a modem by dialing 202-208-1397 if dialing locally or 1-800-856-3920 if dialing long distance. To access CIPS, set your communications software to 19200, 14400, 12000, 9600, 7200, 4800, 2400, or 1200 bps, full duplex, no

parity, 8 data bits and 1 stop bit. The full text of this order will be available on CIPS in ASCII and WordPerfect 5.1 format. CIPS user assistance is available at 202-208-2474.

CIPS is also available through the Fed World system. Telnet software is required. To access CIPS via the Internet, point your browser to the URL address: http://www.fedworld.gov and select the "Go to the FedWorld Telnet Site" button, when your Telnet software connects you, log onto the FedWorld system, scroll down and select FedWorld by typing: 1 and at the command line then typing: /go FERC. FedWorld may also be accessed by Telnet at the address fedworld.gov.

Finally, the complete text on diskette in WordPerfect format may be purchased from the Commissioner's copy contractor, La Dorn Systems Corporation. La Dorn Systems Corporation is also located in the Public Reference Room at 888 First Street, N.E., Washington, D.C. 20426.

Table of Contents

I. Introduction and Summary
II. Public Reporting Burden
III. Background
IV. Discussion
A. Scope of the rule
1. Introduction
2. Functional Unbundling
3. Market-based Rates
a. Market-based Rates for New Generation
b. Market-based Rates for Existing Generation
4. Merger Policy
5. Contract Reform
6. Flow-based Contracting and Pricing
B. Legal Authority
C. Comparability

1. Eligibility to Receive Non-discriminatory Open-Access Transmission
a. Unbundled Retail Transmission and "Sham Wholesale Transactions"
b. Transmission Providers Taking Service Under Their Tariff
2. Service that Must be Provided by Transmission Provider
3. Who Must Provide Non-discriminatory Open-Access Transmission
4. Reservation of Transmission Capacity by Transmission Customers
5. Reservation of Transmission Capacity for Future Use by Utility
6. Capacity Reassignment
7. Information Provided to Transmission Customers
8. Consequences of Functional Unbundling
a. Distribution Function
b. Retail Transmission Service
c. Transmission Provider
1. Taking Service Under the Tariff
2. Accounting Treatment
D. Ancillary Services
1. Specific Ancillary Services
a. Scheduling, System Control and Dispatch Service
b. Reactive Supply and Voltage Control from Generation Sources Service
c. Energy Imbalance Service
(1) Description of Energy Imbalance
(2) Energy Imbalance Bandwidth
2. Ancillary Services Obligations
a. Obligation of a Control Area Utility
b. Obligation to Provide Dynamic Scheduling
c. Obligation As Agent
3. Miscellaneous Ancillary Services Issues
a. Transmission Provider as Ancillary Services Merchant
b. QF Receipt of Ancillary Services
c. Pricing of Ancillary Services

E. Real-Time Information Networks
F. Coordination Arrangements: Power Pools, Public Utility Holding Companies, Bilateral Coordination Arrangements, and Independent System Operators
1. Tight Power Pools
2. Loose Pools
3. Public Utility Holding Companies
4.Bilateral Coordination Arragements
G. Pro Forma Tariff
1. Tariff Provisions That Affect The Pricing Mechanism
a. Non-Price Terms and Conditions
b. Network and Point-to-Point Customers' Uses of the System (so-called "Headroom")
c. Load Ration Sharing Allocation Mechanism for Network Service
(1) Multiple Control Area Network Customers
(2) Twelve Monthly Coincident Peak v. Annual System Peak
(3) Load and Generation "Behind the Meter"
(4) Existing Transmission Arrangements associated with Generating Capacity Entitlements (e.g., "preference power" customer of PMAs)
d. Annual System Peak Pricing for Flexible Point-to-Point Service
e. Opportunity Cost Pricing
(1) Recovery of Opportunity Costs
(2) Redispatch Costs
f. Expansion Costs
g. Credit for Customers' Transmission Facilities
h. Ceiling Rate for Non-firm Point-to-Point Service
i. Discounts
j. Other Pricing Related Issues Not Specifically Addressed in the Final Rule
(1) Demand Charge Credits
(2) In-Kind Transactions
2. Priority For Obtaining Service
a. Reservation Priority for Existing Firm Service Customers

b. Reservation Priority for Firm Point-to-Point and Network Service
c. Reservation Priorities for Non-firm Service
3. Curtailment and Interruption Provisions
a. Pro-rata Curtailment Provisions
b. Curtailment and Interruption Provisions for Non-firm Service
4. Reciprocity Provision
5. Liability and Indemnification
6. Umbrella Service Agreements
7. Other Tariff Provisions
a. Minimum and Maximum Service Periods
b. Amount of Designated Network Resources
c. Eligibility Requirements
d. Two-Year Notice of Termination Provision
e. Termination of Service for Failure to Pay Bill
f. Definition of Native Load Customers
g. Off-System Sales
h. Requirements Agreements
i. Use of Distribution Facilities
j. Losses
k. Modification of Non-rate Terms and Conditions
1. Miscellaneous Tariff Modifications
(1) Ancillary Services
(2) Clarification of Accounting Issues
(a) Transmission Provider's Use of Its System (Charging Yourself)
(b) Facilities and System Impact Studies
(c) Ancillary Services
(3) Miscellaneous Clarifications
(a) Electronic Format
(b) Administrative Changes
8. Specific Tariff Provisions
9. Miscellaneous Tariff Administrative Changes
10. Pro Forma Tariff Compliance Filings
H. Implementation

1. Group 1 Public Utilities
2. Group 2 Public Utilities
3. Clarification Regarding Terms and Conditions Reflecting Regional Practices
4. Future Filings
5. Waiver
I. Federal and State Jurisdiction: Transmission/Local Distribution
J. Stranded Costs
1. Justification for Allowing Recovery of Stranded Costs
2. Cajun Electric Power Cooperative, Inc. v. FERC
3. Responsibility for Wholesale Stranded Costs (Whether to Adopt Direct Assignment to Departing Customers)
4. Recovery of Stranded Costs Associated With New Wholesale Requirements Contracts
5. Recovery of Stranded Costs Associated With Existing Wholesale Requirements Contracts
6. Recovery of Stranded Costs Caused by Retail-Turned-Wholesale Customers
7. Recovery of Stranded Costs Caused by Retail Wheeling
8. Evidentiary Demonstration Necessary—Reasonable Expectation Standard
9. Calculation of Recoverable Stranded Costs
10. Stranded Costs in the Context of Voluntary Restructuring
11. Accounting Treatment for Stranded Costs
12. Definitions, Application, and Summary
K. Other
1. Information Reporting Requirements for Public Utilities
2. Small Utilities
3. Regional Transmission Groups
4. Pacific Northwest
5. Power Marketing Agencies
a. Bonneville Power Administration (BPA)
b. Other Power Marketing Agencies
6. Tennessee Valley Authority
7. Hydroelectric Power
8. Residential Customers

9. Miscellaneous Issues
V. Environmental Statement
A. The Appropriate No-Action Alternative
B. Challenges to Modeling Assumptions
1. Appropriate Base Case
2. Challenge to the Use of Computer Modeling
3. Transmission Assumptions
4. Plant Availabilities and Heat Rates
5. Reserve Margins
6. Northeast MOU
7. Natural Gas Prices
8. Expanded Transmission Analysis
C. Mitigation
D. Emissions Standards Disparity
E. Short-Term Consequences of the rule
G. Cost Benefit Analysis
H. Socioeconomic Impacts
I. Costal Zone Management Act
VI. Regulatory Flexibility Act Certification
A. Docket No. RM95-8-00 (Open Access Final Rule)
1. Public Utilities
2. Non-Public Utilities
B. Docket No. RM94-7-000 (Stranded Cost Final Rule)
1. Public Utilities
2. Non-Public Utilities
VII. Information Collection Statement
VIII. Effective Date

I. Introduction and Summary

On April 24, 1996, the Commission issued Final Rules (Order Nos. 888 *(FERC Statues and Regulations, Regulations Preambles January 1991-June 1996* ¶31,036) and 889 *(FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶31,035) intended to remedy undue discrimination in the provision of interstate transmission services by public utilities and to address the stranded costs that may result from the

transition to more competitive electricity markets.[1] At the heart of these rules is a requirement that prohibits owners and operators of monopoly transmission facilities from denying transmission access, or offering only inferior access, to other power suppliers in order to favor the monopolists' own generation and increase monopoly profits—at the expense of the nation's electricity consumers and the economy as a whole.

The electric utility industry today is not the industry of ten years ago, or even five years ago. While historically it was assumed that local utilities would be the only ones to generate and transmit power for their customers, today there is a broad array of potential competitors to supply power and widespread transmission facilities that can carry power vast distances. But competitors cannot reach customers if they cannot have fair access to the transmission wires necessary to reach those customers. It is against this industry backdrop that the Commission in Order No. 888 exercised its public interest responsibilities pursuant to sections 205 and 206 of the Federal Power Act (FPA), to reexamine undue discrimination in interstate transmission services and the effect of that discrimination on the electricity customers whom we are bound to protect under the FPA.

We here affirm the legal and policy bases on which Order No. 888 is grounded. Utility practices that were acceptable in past years, if permitted to continue, will smother the fledgling

---

[1] Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, 61 FR 21,540 (May 10, 1996), *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶31,036, clarified, 76 FERC ¶61,009 and 76 FERC ¶61,347 (1996). Order No. 889 *(FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶31,035) is an accompanying rule and specific rehearing arguments on that rule will be addressed separately.

competition in electricity markets and undermine the national policies reflected in the Energy Policy Act of 1992 to encourage the development of competitive markets. We firmly believe that our authorities under the FPA not only permit us to adapt to changing economic realities in the electric industry, but also require us to do so, as necessary to eliminate undue discrimination and protect electricity customers. The record supports our conclusion that, absent open access, undue discrimination will continue to be a fact of life in today's and tomorrow's electric power markets. As recent events clearly demonstrate, unbundled electric transmission service will be the centerpiece of a freely traded commodity market in electricity in which wholesale customers can shop for competitively-priced power.

The only way to effectuate competitive markets and remedy discrimination is through readily available, non-discriminatory transmission access. The Commission estimates the potential quantitative benefits from such access will be approximately $3.8 to $5.4 billion per year in cost savings, in addition to the non-quantifiable benefits that include better use of existing assets and institutions, new market mechanisms, technical innovation, and less rate distortion.

Order No. 888 has two central components. The first requires all public utilities that own, operate or control interstate transmission facilities to offer network and point-to-point transmission services (and ancillary services) to all eligible buyers and sellers in wholesale bulk power markets, and to take transmission service for their own use under the same rates, terms and conditions offered to others. In other words, it requires non-discriminatory (comparable) treatment for all eligible users of the monopolists' transmission facilities. The non-discriminatory services required by Order No. 888, known as open-access services, are reflected in a *pro forma* open-access tariff contained in the Rule. The rule also requires functional

separation of the utilities' transmission and power marketing functions (also referred to as functional unbundling) and the adoption of an electric transmission system information network.

The second central component of Order No. 888 was to address whether and how utilities will be able to recover costs that could become stranded when wholesale customers use the open-access tariffs, or FPA section 211 tariffs,[2] to leave their utilities' power supply systems and shop for power elsewhere. Because of competitive changes occurring at the retail level, as numerous states have begun retail transmission access programs, Order No. 888 also clarifies whether and when the Commission may address stranded costs caused by retail wheeling and the extent of the Commission's jurisdiction over unbundled retail transmission. The Commission further addresses the circumstances under which utilities and their wholesale customers may seek to modify contracts made under the old regulatory regime, taking into account the goals of reasonably accelerating customers' ability to benefit from competitively priced power and at the same time ensuring the financial stability of electric utilities during the transition to competition.

137 entities filed requests for rehearing and/or clarification of Order No. 888. While these parties raise a variety of arguments—including legal, policy, and technical arguments—the majority (including a majority of public utilities) agree that we need to harness the benefits that competitive electricity markets can bring to the nation. The disagreements primarily focus on the mechanics of how we should do this, who should

---

[2] Under section 211 of the FPA, the commission, on a case-by-case basis upon application by an eligible customer, may order both public utilities and non-public utilities that own or operate transmission facilities used for the sale of electric energy at wholesale to provide transmission services to the applicant if it finds it is in the public interest to issue such order.

pay the costs of the transition to competition, and how long the transition should take.

First, parties disagree on what is necessary to remedy undue discrimination and to develop truly competitive wholesale markets. Many focus specifically on the tariff terms and conditions of good transmission access and seek changes in the Order No. 888 *pro forma* tariff. In response to these types of rehearing arguments, the Commission has fine-tuned or changed some of the *pro forma* tariff terms and conditions to better ensure that they do not permit discrimination and that they result in well-functioning markets. Other petitioners focus on additional structural changes which they believe are necessary, such as mandatory corporate restructuring (divestiture of generation assets) or mandatory creation of independent transmission system operators (ISOs). With regard to restructuring, the Commission continues to believe that functional unbundling of the utility's business, not corporate divestiture or mandatory ISOs, is sufficient to remedy undue discrimination at this time.

The most contentious arguments raised on rehearing involve how we deal with the transition costs associated with moving to competition. Some utilities have invested millions of dollars in facilities and purchased power contracts based on an explicit or implicit obligation to serve customers and the expectation that those customers would remain on their systems for the foreseeable future. These utilities face so-called "stranded costs" which, if not recovered from the customers that caused the costs to be incurred, could be shifted to other customers.

There are two basic categories of rehearing arguments regarding stranded cost recovery. Most utilities want a guarantee from this Commission that they will recover all stranded costs, whether caused by losing retail customers or wholesale customers. Many customers, on the other hand, want to be able to abrogate existing power supply contracts so that they can

immediately leave their current suppliers' systems and shop for cheaper power elsewhere, without paying the sunk costs that their suppliers incurred on their behalf.

In response to these diverse arguments, the Commission has struck a reasonable balance that, for certain defined circumstances, permits utilities the opportunity to seek extra-contractual recovery of stranded costs from their departing customers and permits customers the opportunity to make a showing that their contracts should be shortened or terminated. Based on our experience in the natural gas area, we have learned that it is critical to address these issues early, but we also have chose an approach different from that taken in the gas area because of the different circumstances facing the electric industry.

In balancing the wide array of interests reflected in the rehearing petitions, we have made a number of clarifications and granted rehearing on some issues, but we reaffirm the core elements and framework of Order No. 888. Since the time the final rules issued, as discussed in section III, the pace of competitive change has continued to escalate in the industry at both the wholesale and retail levels as competitors, customers and state regulatory authorities aggressively seek ways to lower the price of electricity. We therefore believe it is all the more critical that we remedy undue discrimination in interstate transmission services now, and that we do so generically, if we are to fulfill our responsibilities under the FPA to protect consumers and provide fair and orderly transition to new competitive markets.

Finally, with respect to environmental issues associated with this rulemaking, certain parties on rehearing continue to challenge the adequacy of our Final Environmental Impact Statement (FEIS). The central issues are whether the Final Rule will increase emissions or nitrogen oxides (NO_x) from certain

fossil-fuel fired generators, while could affect air quality in downwind areas to which these emissions may be carried, and the Commission's authority to mitigate environmental consequences.

We deny rehearing on the environmental issues raised and affirm our conclusion that we have satisfied our obligations under NEPA. As discussed in detail in the Final Rule, this rulemaking is expected to slightly increase or slightly decrease total future No_x emissions, depending on whether competitive conditions in the electric industry favor the utilization of natural gas or coal as a fuel for the generation of electricity. We also examined mitigation options over the longer term, and found that the preferred approach for mitigating any adverse environmental consequences would be for the Environmental Protection Agency (EPA) and the states to address the problem through regulatory authorities available under the Clean Air Act. The petitions for rehearing have not persuaded us to change this approach. Indeed, we note that since the issuance of Order No. 888, the EPA has concluded that the rule is unlikely to have any immediate significant adverse environmental impact and thus concurred that the Commission's analysis is adequate under NEPA. We further note that EPA has recently taken steps under the Clean Air Act to address NO/x/ emissions as part of a comprehensive emissions control program, along the lines endorsed by the Commission in the EIS.

In summary, the Commission believes that our authorities under the FPA not only permit us to adapt to changing economic realities in the electric industry, but also requires us to do so to eliminate undue discrimination and protect electricity customers. The measures required in Order No. 888 are necessary to remedy undue discrimination in interstate transmission services and provide an orderly and fair transition to competitive bulk power markets.

To assist the reader, we provide below a section-by-section summary of key elements of this Order on Rehearing.

Scope of the Rule

In this section we discuss petitions to rehear our requirement that transmission and power sales services be contracted for separately (unbundled). We affirm that this requirement is a reasonable and workable means of assuring non-discriminatory open-access transmission. In doing so we refuse invitations to require that utilities under our jurisdiction divest themselves of generation or transmission assets. We do, however, make an important clarification involving how we will deal with existing contracts that contain so-called *Mobile-Sierra* clauses (clauses under which one or both parties agreed not to seek modification of contract terms unless they could show that it is contrary to the public interest not to permit the modification).

In Order No. 888 we concluded that contracts would not be abrogated by operation of the Rule. Instead, preexisting contracts would continue to be honored until such time as they were revised or terminated. We also found that those who were operating under pre-existing requirements contracts containing *Mobile-Sierra* clauses would nonetheless be allowed to seek reform of the contracts on a case-by-case basis. On rehearing we affirm that public utilities will be allowed to file to amend their *Mobile-Sierra* contracts for the limited purpose of providing an opportunity to seek recovery of stranded costs, without having to make a public interest showing that such cost recovery should be permitted. However, these utilities will have the burden, on a case-by-case basis, of showing that they had a reasonable expectation of continuing to serve the departing customer after the contract term. We clarify that if the utilities under such contracts seek to modify provisions that do not relate to stranded costs, they will have the burden of showing that the provisions are contrary to the public interest.

We here make clear that, in turn, customers will be allowed to file to maned their *Mobile-Sierra* conflicts to modify any contract term or to terminate the contract, without having to make a showing that the contract terms are contrary to the public interest. Instead, customers seeking modifications must demonstrate that the provisions they wish modified are no longer "just and reasonable." We affirm our conclusion in the Final Rule that if a customer seeks to shorten or eliminate the term of its contract, however, any contract modification approved by the Commission will provide for appropriate stranded cost recovery by the customer's supplying utility.

These various provisions meet the twofold need to deal with stranded costs and the contracts under which those costs were incurred. However, as described in Order No. 888, the opportunity to reform *Mobile-Sierra* contracts extends only to a limited set of contracts—those entered into on or before July 11, 1994, for requirements power.

Comparability

In this section we deal with those requesting rehearing of our conclusions regarding what "comparable" service is, who is eligible for that service, and how it is to be implemented. We affirm our finding that, as a matter of law, we have jurisdiction over the rates, terms and conditions of unbundled transmission service provided to retail customers. We also clarify that we have authority to order "indirect" unbundled retail transmission services and that if such transmission is ordered by us in the future, or if it is provided voluntarily, otherwise eligible customers may obtain such service under the open-access tariff. We expect public utilities to provide such service in the future and, if they do not, we will not hesitate to order it.

We modify in two respects the definition of who is eligible for open-access transmission service. First, we clarify that, with

respect to service that this Commission is prohibited from ordering by section 212(h) of the Federal Power Act (retail wheeling directly to an ultimate consumer and "sham" wholesale wheeling), entities are eligible for such service under the tariff only if it is provided pursuant to a state requirement or is provided voluntarily. Second, we clarify that retail customers taking unbundled service pursuant to a state requirement (i.e., direct retail service) are eligible for such service only from those transmission providers that the state orders to provide service. These changes are made to make clear that our rules cannot be used to circumvent the proscriptions placed on the Commission against ordering direct retail wheeling.

Ancillary Services

In this section we deal with petitions to rehear our definitions of ancillary services—those services such as scheduling, voltage control, and supplemental reserve service that must or can attend the providing of transmission service—as well as the provisions involving these services. We reaffirm that tariffs must separately state the charges for these services. We do modify some of the definitions of these services to conform to industry needs and practices. Most importantly, we make clear that the transmission provider's sale of ancillary services associated with providing basic transmission service is not a wholesale merchant function and thus does not violate the standards of conduct imposed with Order No. 889.

Coordination Arrangements

The requirement to provide non-discriminatory open-access transmission applies to any agreement between utilities that contains transmission rates, terms or conditions. This includes pooling arrangements and agreements between companies contracting to provide each other mutually beneficial transmission services. In Order No. 888 we laid out rules under

which the open-access comparability requirements would apply to tight and loose power pools, public utility holding companies and bilateral coordination agreements. We also set out principles that would govern our approval of independent system operator (ISO) agreements.

In this section we affirm the rules governing coordination agreements. In doing so we clarify the definition of "loose pool." we also make clear that, unlike in other situations where we require utilities to provide not only the services they provide themselves but those they could provide themselves, we will require members of loose pools to offer to third parties only those transmission services that they provide themselves under their pool-wide agreements.

We also reaffirm our strong commitment to the concept of ISOs and the ISO principles described in Order No. 888. In doing se we reject arguments that we should require that ISOs be formed. At the same time, we emphasize that while there is no "cookie-cutter" approach to forming an acceptable ISO, the requirement of fair and non-discriminatory rules of governance (Principle One) and the requirement that ISO employees have no financial interest in the economic interests of power marketers—backed by strict conflict of interest provisions—(Principle Two) are fundamental to our approving any ISO.

Pro Forma Tariff Provisions

The *pro forma* tariff is the basic mechanism implementing the requirements of comparable open-access transmission. It provides the details of the transmission service obligations imposed on jurisdictional utilities by the Rule. On rehearing we affirm most of the provisions set out in Order No. 888 for the *pro forma* tariff. We do make changes to conform the *pro forma* tariff to changes adopted under other sections (for example, the definition of "eligible customer").

The rehearing petitions raised many questions about how particular aspects of the tariff will work. For the most part, these questions cannot be answered generically, but must be resolved on a case-by-case basis in the context of specific fact situations. However, the petitions brought to light issues that require clarifications and in some cases revisions to the tariff. The most significant of these involve discounting practices, provisions governing priority of service and curtailment, and the reciprocity provision.

Discounting practices. Originally, we provided different rules depending upon whether the transmission provider was offering a discount to itself or an affiliate or offering a discount to a non-affiliate. In response to the rehearing petitions, we are making three significant changes to the discounting requirements to better permit the ready identification of discriminatory discounting practices while also providing greater discount flexibility.

First, any discount offered on transmission services (including supporting ancillary services) by a transmission provider or requested by any customer must now be made only over the OASIS. With this change, all will have the same, timely access to discounted services. In making this change, we clarify that a transmission provider may limit its discounted service to particular time periods.

Second, once the provider and customer agree on a discount, the details on the discounted service—the price, points of receipt and delivery, and length of service—must be immediately posted on the OASIS.

Third, we revise our rule respecting what other transmission paths must be offered at a discount. Originally, in Order No. 888, we required that when a discount was offered over one path, the transmission provider would have to provide that discount over

all other unconstrained paths on its system. We will no longer require this. Instead, the discount will be limited to those unconstrained paths that go to the same point(s) of delivery as the discounted service being provided on the transmission provider's system. The discount will extend for the same time period and must be offered to all transmission service customers.

Priority and Curtailment. We affirm the right of first refusal policy that reservation priority continues for firm service customers served under a contract of one year or more. We also affirm that curtailment must be made on a pro-rata basis and clarify that non-firm point-to-point service is subordinate to firm service. However, we clarify that the pro-rata curtailment requirement extends to only those transactions that alleviate the constraint.

Reciprocity. In Order No. 888 we conditioned the use of a public utility's open-access service on the agreement that, in return, it is offered reciprocal service by non-public utilities that own or control transmission facilities. Such reciprocal service does not have to be through an open-access tariff, i.e., a tariff available to all eligible customers, but may be limited to those public utilities from whom the non-public utility obtains open-access service. We affirm the reciprocity condition. In doing so, however, we make several clarifications.

First, a public utility is free to offer transmission service to a non-public utility without requiring reciprocal service in return. In other words, it may voluntarily waive the reciprocity condition. However, if it chooses to do so, transmission service must be provided through the *pro forma* tariff. Alternatively, bilateral agreements for transmission service provided by the public utility will not be permitted.

Second, we clarify that under the reciprocity condition a non-public utility must agree to offer the Transmission Provider any

transmission service the non-public utility provides or is capable of providing on its system. This means that the non-public utility undertaking reciprocity must have an OASIS and must operate under the standards of conduct imposed under Order No. 889 unless it is granted a waiver by the Commission or, where appropriate, by a regional transmission group (RTG) of which it is a member. We also clarify that a non-public utility cannot avoid its responsibilities by obtaining transmission service through other transmission customers. Further, the seller as well as the buyer in the chain of a transaction involving a non-public utility will have to comply with the reciprocity condition.

Third, we adhere to our decision not to treat generation and transmission (G&T) cooperatives and their member distribution cooperatives as a single unit. Thus, the reciprocity provision extends to the G&T Cooperative and not to its member distribution cooperatives.

Fourth, we clarify the "safe harbor" provision under which a non-public utility may get a Commission decision that its transmission tariff suffices to meet reciprocity. A non-public utility may limit the use of any reciprocity tariff that it voluntarily files at the Commission to those transmission providers from whom the non-public utility obtains open-access service. A non-public utility also may satisfy reciprocity through bilateral agreements with a public utility. As a related matter, if a public utility believes a non-public utility is violating the reciprocity condition, it may file with the Commission a petition to terminate its service to the non-public utility.

Fifth, we clarify that non-public utilities may include stranded cost provisions in their reciprocity tariffs.

Sixth, the order on rehearing removes the term "interstate" from the reciprocity provisions. This is to make clear that reciprocity applies even to those who do not own or control

interstate transmission facilities, i.e., foreign utilities and those located in the ERCOT region of Texas.

As to local furnishing bonds held by some public utilities, we clarify that all costs associated with the loss of tax-exempt status of those bonds caused by providing open-access transmission service are properly considered costs of providing that service. This includes costs of defeasing, redeeming, and refinancing those bonds.

Other Clarifications. In this order on rehearing we take the opportunity to clarify various other tariff provisions. Among these: Transmission providers do not have to take service under the open-access tariff for transmitting power purchased on behalf of their bundled retail customers. Also, the ability to reserve capacity to meet the reliability needs of a transmission provider's native load applies equally to present transmission and transmission that is built on the future.

Implementation

On rehearing, we make no substantive changes to the implementation provisions originally required under Order No. 888. For the most part, the implementation process has been completed. Utilities have made the requisite tariff and compliance filings and public and non-public utilities have, through other orders, been provided guidance as to obtaining waivers of Order No. 888 and Order No. 889 requirements.

We emphasize that we do not require the abrogation of existing contracts. Rather, the Rule requires only that transmission providers offer transmission under the open-access tariff in addition to existing service obligations. Commitments made under existing contracts will continue. Of course, both transmission providers and their customers may seek to revise

the terms and conditions of existing contracts by making the necessary filings as appropriate, under sections 205 and 206 of the Federal Power Act.

State and Federal Jurisdiction

On rehearing we reaffirm our decision that when transmission services is provided to serve retail customers apart from any contract for the retail sale of power, i.e., when it is provided on an unbundled basis, that transmission service is under our jurisdiction. In today's market, and increasingly in the future as more states adopt retail wheeling programs, retail transactions are, and will be, broken down into products that are sold separately—transmission and generation—and sold by different entities. The exercise of our jurisdiction over the rates, terms and conditions of unbundled retail transmission will, therefore, become more important. We also recognize that states have jurisdiction over facilities used for local distribution.

On rehearing, we also reaffirm the seven-factor test of Order No. 888 to distinguish transmission under our jurisdiction from state-jurisdictional local distribution. In doing so, we recognize that our test does not resolve all possible issues. There may be other factors that should be taken into account. The test, therefore, is designed for flexibility to include unique local characteristics and usages. To that end, we will continue to defer to state findings on these matters.

In addition, we clarify that states have the authority to determine the retail marketing areas of the electric utilities within their respective jurisdictions. We also recognize that states have the concomitant authority to determine the end-user services these utilities provide.

Stranded Costs

On rehearing, we reaffirm our basic decisions surrounding the recovery of stranded costs. Utilities will be allowed the opportunity to seek to recover legitimate, prudent, and verifiable wholesale stranded costs. This opportunity is limited to costs associated with serving customers under wholesale requirements contracts executed on or before July 11, 1994 that do not contain explicit stranded cost provisions; and costs associated with serving retail-turned-wholesale customers.

We clarify that we will consider on a case-by-case basis whether to treat a contract extended or renegotiated without a stranded cost provision as an existing contract for stranded cost purposes.

In each case, the opportunity to seek stranded costs is limited to situations in which there is a direct nexus between the availability and use of a Commission-required transmission tariff and the stranding of the costs. The Rule does not allow the recovery of costs that do not arise from the new, accelerated availability of non-discriminatory transmission access.

The Commission also reaffirms its decision that stranded costs should be recovered from the customer that caused the costs to be incurred. The Commission is not requiring other remaining customers, or the utility, to shoulder a portion of its stranded costs that meet the requirements for recovery.

The Commission, as described in Order No. 888, will be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers. With respect to such cases, we have made several changes.

First, the Commission has reconsidered its decision respecting cases involving existing municipal utilities that annex retail

customer service territories. Under Order No. 888, we found that in such cases the Commission should not be the primary forum for determining stranded cost recovery. On rehearing we now find that such cases should fall within our province.

Second, we clarify that the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers applies regardless of whether the customer or its new supplier is the one requesting and contracting for the transmission service. To this end, we have revised the definition of "wholesale stranded cost."

With respect to the recovery of stranded costs caused by unbundled retail wheeling, we affirm that the only circumstance in which we will entertain requests for these types of costs is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required. We clarify that if a state regulatory authority has in fact addressed such costs, regardless of whether it has allowed full recovery, partial recovery or no recovery, utilities may not apply to the Commission to recover stranded costs caused by the retail wheeling.

Other

In this section we resolve questions concerning our information reporting requirements, regional transmission groups, and the special situations posed by utilities in the Pacific Northwest and by the federal power marketing and similar agencies. Here we make some minor clarifications but make no significant changes to Order No. 888.

We are not persuaded that the information reporting requirements need to be changed at this time. Finally, we reject arguments that would have us fix generically any particular rate

methodology for providing open-access transmission service under the *pro forma* tariff.

II. Public Reporting Burden

This order on rehearing issues a number of minor revisions to the Final Rule. We find, after reviewing these revisions, that they do not, on balance, increase the public reporting burden.

The Final Rule contained an estimated annual public reporting burden based on the requirements of the Open Access Final Rule and the Stranded Cost Final had the opportunity to protest the compliance filings when they were tendered,[447] but these customers also have the right to file section 206 requests to change these tariffs at any time. In addition, Blue Ridge's request that customers be given 45 days to respond to compliance filings instead of 15 days is moot. In an order issued July 2, 1996,[448] we took three actions to address this concern: (1) we gave entities 30 days, instead of 15 days, to respond to Order No. 888 compliance filings; (2) we agreed to post an electronic version of all Order No. 888 compliance filings on the Commission's Electronic Bulletin Board; and (3) we required all public utilities making a compliance filing to also serve a copy of their filing on electronic diskette to any eligible customer or state regulatory agency requesting a copy. We believe that these actions not only provided all interested parties with access to the compliance filings more quickly, but also provided these parties sufficient

[447] We do note that most of these concerns have been addressed in our orders dealing with the compliance filings on non-rate terms and conditions. *See, e.g., Atlantic City Electric Company, et al.*, 77 FERC ¶61,144 (1996); *Allegheny Power System, Inc., et al.*, 77 FERC ¶61,266 (1996).

[448] 76 FERC ¶61,009, at pp. 61,026-27 (1996) (July 2 Order).

time to analyze the information once they received it.[449] Moreover, the time periods provided for making and responding to Order No. 888 compliance filings have expired.

With regard to Blue Ridge's first clarification request, we provide the following guidance. Utilities that had pending open-access filings at the time that the Final Rule was implemented had the non-price terms and conditions of those pending tariffs superseded by their Order No. 888 compliance filings. Any customer concerns about the non-rate tariff terms and conditions in the compliance filing should be raised in the compliance docket, and any future customer concerns should be raised in a separate, future section 206 complaint filed by the customer.

Furthermore, we reject Indianapolis P&L's rate issue because, if this utility believes that it operates under special circumstances that requires it to use "non-conforming" pricing methods, it is free to file such a proposal under section 205. The merits of Indianapolis P&L's arguments are more appropriately addressed in such a section 205 proceeding. The Commission will not alter its generic policy (which is the subject of this rulemaking) merely to address the particular needs of one party.

In addition, with regard to both of Indianapolis P&L's concerns, we note that pursuant to the Commission's July 2 Order, the Commission indicated that it would not address waiver requests in a generic proceeding and that parties would have to file such requests separately for separate docketing. We

[449] We also note that utilities were required in Order No. 888 to explicitly identify any regional practices in their compliance filings.

further note that Indianapolis P&L filed a separate waiver request on July 9, 1996, which was docketed as OA96-81.[450]

We also reject Union Electric's argument that the final rules violate procedural due process. Union Electric has had every opportunity to raise arguments with regard to every step in the Commission's derivation and implementation of the final rules. Moreover, with regard to Union Electric's claim that it was given an adequate amount of time to comprehend and implement the final rules, we note that virtually every public utility, including Union Electric, complied with the Open Access Rule on a timely basis, and there have been very few complaints that the rules are hard to comprehend.

I. *Federal and State Jurisdiction: Transmission/Local Distribution*

In the Final Rule, the Commission explained that after reviewing the extensive analysis of the FPA, legislative history, and case law contained in both the initial Stranded Cost NOPR and in the Open Access NOPR, and the comments received on that analysis, it reaffirmed its assertion of jurisdiction over the transmission component of an unbundled interstate retail wheeling transaction.[451] The Commission also reaffirmed and clarified its determinations regarding the tests to be used to determine what constitute Commission-jurisdictional transmission facilities and what constitute state-jurisdictional

[450] By order issued September 1, 1996, the Commission denied Indianapolis P&L's requested waiver of all the requirements of Order No. 888. On October 8, 1996, Indianapolis P&L sought rehearing of that order and a stay of the requirements of Order No. 888. These pleadings are now pending before the Commission.

[451] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,780-85; mimeo at pp. 427-42.

local distribution facilities in situations involving unbundled wholesale wheeling and unbundled retail wheeling.

The Commission also explained that where states unbundle retail sales, it will give deference to their determinations as to which facilities are transmission and which are local distribution, provided that the states, in making such determinations, apply the seven criteria discussed in the NOPR and reaffirmed by the Commission. In addition, the Commission clarified that there is an element of local distribution service in any unbundled retail transaction, and further clarified other aspects of its jurisdictional ruling to preserve state jurisdiction over matters that are of local concern and will remain subject to state jurisdiction if retail unbundling occurs.

The Commission reaffirmed its legal determination that if unbundled retail transmission in interstate commerce occurs voluntarily by a public utility or as a result of a state retail access program, this Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission. The Commission found compelling the fact that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.

The Commission further explained that when a retail transaction is broken into two or more products that are sold separately, the jurisdictional lines change. In this situation, the Commission emphasized that the state clearly retains jurisdiction over the sale of the power, but the unbundled transmission service involves only the provision of "transmission in the interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission.

The Commission recognized that in asserting jurisdiction over unbundled retail transmission in interstate commerce by public

utilities, it was in no way asserting jurisdiction to order retail transmission directly to an ultimate consumer. It explained that its assertion of jurisdiction is that if unbundled retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission and public utilities offer such transmission must comply with the FPA by filing proposed rate schedules under section 205.

The Commission further clarified that nothing in its jurisdictional determination changes historical state franchise areas or interferes with state laws governing retail marketing areas of electric utilities. It explained that while its jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over transmission in interstate commerce by public utilities.

The Commission also adopted a new section 35.27(b) as follows:

> Nothing in this part (i) shall be construed as preempting or affecting any jurisdiction a state commission or other state authority may have under applicable state and federal law, or (ii) limits the authority of a state commission in accordance with state and federal law to establish (a) competitive procedures for the acquisition of electric energy, including demand-side management, purchased as wholesale, or (b) non-discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

With respect to the Commission's adoption of the Open Access NOPR's function/technical tests for determining what

facilities are Commission-jurisdictional facilities used for transmission in interstate commerce and what facilities are state-jurisdictional local distribution facilities, the Commission concluded that it could not divine a bright line for unbundled retail transmission by the public utility that previously provided bundled retail service to the end user. The Commission added that the limited case law, including *Connecticut Light & Power Company v. FPC (CL&P) and Federal Power Commission v. Southern California Edison Company (the Colton case)*,[452] supports a case-by-case determination.[453] Accordingly, the Commission stated that its technical test, with its seven indicators, will permit reasoned factual determinations in individual cases.

The Commission made two clarifications regarding local distribution in the ontext of retail wheeling. First, it explained that even if its technical test for local distribution facilities were to identify no local distribution facilities for a specific transaction, states have authority over the service of delivering electric energy to end users. Second, the Commission explained that through their jurisdiction over retail delivery services, states have authority not only to assess retail stranded costs but also to assess charges for so-called stranded benefits, such as low-income assistance and demand-side management.

Thus, under this interpretation of state/federal jurisdiction, the Commission explained, customers have no incentive to structure a purchase so as to avoid using identifiable local distribution

---

[452] 324 U.S. 515 (1945) (CL&P); 376 U.S. 205 (1964) (Colton).

[453] The Commission included a detailed legal analysis in appendix G to Order No. 888. The Commission explained that it was particularly persuaded by the Supreme Court's Statement that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. See CL&P, 324 U.S. at 534-35).

facilities in order to bypass state jurisdiction and thus avoid being assessed charges for stranded costs and benefits.

The Commission further determined that it is appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs.

In instances of unbundled retail wheeling that occurs as a result of a state retail access program, the Commission indicated that it will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[454] Moreover, the Commission indicated that it will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

As a means of facilitating jurisdictional line-drawing, the Commission stated that it will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, the Commission explained that, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the

[454] In order to give such deference, the Commission noted its expectation that state regulators will specifically evaluate the seven indicators and any other relevant facts and make recommendations consistent with the essential elements of the Rule.

principles established in the Final Rule, the Commission indicated that it will defer to such classifications and/or cost allocations.

Furthermore, the Commission stated that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances. The Commission explained that when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes—a transmission component and a local distribution component. It again emphasized that the Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component. Thus, the Commission stated, the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. However, the Commission added, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a separate retail transmission tariff[455] to accommodate the design and special needs of such programs. In such situations, the Commission indicated that it will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open-access policies and comparability principles reflected in the tariff prescribed by the Final Rule. In addition, the Commission indicated that the rates must be consistent with its Transmission Pricing Policy Statement, and the guidance set forth in Order No. 888 concerning ancillary services.[456]

[455] The Commission noted that such a tariff could be different from the tariff that applies to wholesale customers, but that such tariff would still be filed with the Commission under FPA section 205.

[456] In applying the principles of the Final Rule to retail transmission tariffs, the Commission emphasized that it clearly cannot order retail wheeling directly to an ultimate consumer. (citing FPA section 212(h)).

The Commission also expressed concern, just as it did with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, the Commission reaffirmed its conclusion that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. Moreover, the Commission indicated that it will address these transactions on a case-by-case basis.

Rehearing Requests

Oppose Commission Assertion of Jurisdiction Over Unbundled Retail Transmission

Several state commissions indicate that, recognizing that the case law is not dispositive concerning the question of unbundled retail transmission services (either because the cases do not involve the transmission of power to retail customers or "fence off" local distribution from federal regulation); at least one court (*Wisconsin-Michigan Power Company v. FPC*, 197 F.2d 472 (7th Cir. 1952), *cert. denied*, 345 U.S. 934 (1953)) explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services.[457] Thus, they argue, the Commission should apply the wholesale versus retail analysis to the question of unbundled retail transmission.

IL Com asserts that retail transmission by a public utility directly to an end user has always (even before the FPA was enacted) been subject to regulation by the states. It contends that no change in law has occurred which justifies the Commission's

[457] *E.g.*, NARUC, WI Com, WY Com.

claim of expanded jurisdiction. Moreover, it disagrees with the Commission's conclusion that the unbundled delivery by the previous public utility generation supplier directly to an end user is in interstate commerce. It argues that the FPA was never intended to disturb the jurisdiction of state regulators that existed prior to its passage and that retail transmission of electric energy by a public utility to an end user was under state jurisdiction before the *Attleboro* decision and has remained under state jurisdiction in the over sixty years following *Attleboro*. Even after unbundling, according to IL Com, transmission to a retail customer still involves a retail sale of transmission.

NARUC and VA Com assert that the legislative history provides little support for the Commission's conclusion that the act of unbundling generation from delivery serves to shift jurisdiction from a state commission to the Commission. If anything, they contend, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services. They assert that the Commission should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer are subject to the jurisdiction of the state commission regulating the utility, regardless of the identity of the party generating or reselling the power or the facilities used to transport the power.

NARUC asserts that the Commission did not address a point raised in NARUC's reply comments as to how the removal of generation serves to unbundle the retail delivery function into separate transmission and distribution services. It maintains that the Commission simply assumes that a resulting transmission

transaction is created when power is sold to a retail consumer by someone other than the utility delivering the power.[458]

MI & NH Coms ask the Commission to vacate those portions of the Rule that find that the Commission has jurisdiction over the transmission component of an unbundled retail sale in a local retail wheeling transaction. They assert that the Commission should confine its activity to wholesale transactions or those interstate transactions that do not implicate matters to local concern. They argue that the dual federal/state regulatory scheme establishes that Congress' intent is that state regulation of retail wheeling is *not* preempted by federal law as established in FPA section 201. They oppose unnecessary federal intrusion into local matters under a one-size-fits-all approach and assert that the retail wheeling initiatives in New Hampshire and Michigan are tailored to the unique utility environment in each state.

Central Illinois Light argues that unbundling of retail electric service does not change the states' longstanding jurisdiction over retail electric service and local distribution, even when that service involves the use of transmission in interstate commerce. It asserts that 201(b)(1) ("transmission of electric energy in interstate commerce") cannot be read in a vacuum.

MN DPS & MN Com and OH Com assert that the Commission should have no role in the regulation of retail services, be they bundled or unbundled. They argue that, in refusing to grant the Commission authority over retail wheeling, Congress left jurisdiction over retail electric service to the states.

---

[458] *See also* IA Com (use of a utility's transmission system to serve its own retail customers is a bundled part of the retail sale transaction, which supports a simpler jurisdictional test holding that a movement of power by the last utility in any chain of delivery to a retail customer is a distribution transaction).

They conclude that the Final Rule contains insufficient legal and/or policy justification for the Commission's assertion of jurisdiction over unbundled retail transmission services.

MN DPS & MN Com assert: "FERC bases its usurpation of state authority over retail transmission rates on its claim that balkanization would occur without the assertion of FERC authority. Therefore, the parties are entitled to rehearing so that this essential issue can be further analyzed." (MN DPS & MN Com at pp. 1-3).

FL Com argues that the Commission has not justified why the act of unbundling prices expands the Commission's jurisdiction into retail marketing areas. It argues that Section 212(g) of the FPA has the effect of prohibiting the Commission from usurping existing state jurisdiction over retail transmission service, whether bundled or unbundled. According to FL Com. FERC's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. It supports wheeling in jurisdiction for state commissions and wheeling out and wheeling through jurisdiction for the Commission.

IN Com opposes federalization of retail wheeling transactions within a state's boundaries as contrary to the FPA's legislative history and case law.

NJ BPU asserts that by claiming jurisdiction over unbundled retail transmission, the Commission is creating a disincentive for states to implement retail access because, by ordering retail access, the states may be relinquishing their jurisdiction over unbundled retail transmission terms and conditions—jurisdiction that they would maintain under a bundled scenario.[459] PA Com argues that the Commission does not have the authority to order

---

[459] *See also* PA Com.

retail wheeling and that the jurisdictional formula is challengeable on engineering and legal grounds. It concludes that the Commission does not have jurisdiction over unbundled interstate retail transmission service, PA Com notes that the 1996 House and Senate hearings have raised the question whether the Commission has the statutory authority to restructure the electric industry. PA Com questions the Commission's definition of the "traditional tasks of state and federal regulators" on the basis of section 201(b) of the FPA, the Supremacy Clause, and the Tenth Amendment of the U.S. Constitution.

Support Broader Assertion of Jurisdiction by the Commission Over Retail Wheeling

NY Utilities declare that the Commission has jurisdiction over retail wheeling from the source to the load, but does not have jurisdiction over transmission in bundled retail service. They assert that the Commission's reliance on state jurisdictional local distribution as a predicate to abstain from allowing retail wheeling stranded cost recovery is without foundation. They further assert that a unique element that sets local distribution apart from transmission is not the size of the facility or the length of travel, but that transportation is bundled with a retail sale. According to NY Utilities, the plain meaning of the FPA shows that local distribution is bundled retail service. They claim that the legislative history, to the extent necessary, and court cases support FERC jurisdiction over all aspects of retail wheeling, but makes clear that the Commission cannot regulate bundled retail service. They add that the NGA also demonstrates that local distribution means bundled retail service.

Commission Conclusion

In concluding that this Commission has exclusive jurisdiction over the rates, terms and conditions of unbundled retail transmission by public utilities in interstate commerce, the

Commission in Order No. 888 thoroughly examined the statutory language of the FPA and its legislative history, and relevant FPA and NGA case law. While the state commissions on rehearing would like us to draw a bright line that gives them, to varying degrees, jurisdiction over retail interstate transmission by public utilities, no party on rehearing has raised any legislative history or case law that was not previously considered and that would support the proposition that states have jurisdiction over any unbundled transmission in interstate commerce. As explained below, we reaffirm our jurisdictional interpretation on rehearing and believe that it is supported by the recent decision in *United Distribution Companies v. FERC.*[460]

Many of the rehearing arguments focus on the fact that states historically (even prior to the FPA) regulated retail transmission insofar as it was a component of bundled electric service to an end user, and they argue that by asserting jurisdiction over unbundled retail transmission, the Commission is somehow "taking away" jurisdiction the states previously had. The flaw in these arguments is their inherent assumption that jurisdiction over transmission service turns upon the question of whether the transmission service is being provided for "wholesale" or "retail" power sales. That is not the case. The question of jurisdiction rather turns upon the extent of the Commission's exclusive jurisdiction over transmission in interstate commerce under the FPA. The fact that states historically regulated most retail transmission service as a part of a bundled retail power sale is not the result of a legal requirement; it is the practical result of the way electricity has historically been bought and sold. However, the shape of power sales transactions is rapidly changing. Rather than claiming "new" jurisdiction; the Commission is applying the same statutory framework to a

---

[460] 88 F.3d 1105, 1152-53 (1996) (United Distribution Companies).

business environment in which, as discussed below, retail sales and transmission service are provided in separate transactions.

In the past, retail sales occurred almost exclusively on a bundled basis (i.e., the same entity provided a delivered product called electric energy and transmission was part and parcel of that product). The FPA clearly reserves the right to regulate retail sales of electric energy to the states. As we explained in the Final Rule, however, in today's markets, and increasingly in the future as more states adopt retail wheeling program, retail transactions are being broken into products that are being sold separately; transmission and generation. Moreover, these products are being sold increasingly by two or more different entities. For example, a transaction may involve transmission service from one or more transmission providers who move power from a distant generation supplier, over the interstate transmission grid, to an end user. Because these types of products and transactions were not prevalent in the past, the jurisdictional issue before us did not arise and, contrary to IL Com's argument, the Commission cannot be viewed as "disturbing" the jurisdiction of state regulators prior to and after the *Attleboro* case.[461]

As we also explained in the Final Rule, the legislative history of the FPA and the relevant case law similarly reflect the historical market structure in which electricity and transmission generally were bought on a bundled basis.[462] Today's unbundled world simply was not contemplated and the cases do not resolve dispositively this jurisdictional issue. The case law focuses primarily on the bright line between wholesale sales and retail

---

[461] *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927).

[462] The case law is addressed extensively in appendix G to the Final Rule and will not be repeated here.

sales of energy, and transmission in interstate as opposed to intrastate commerce. It does not address unbundled retail interstate transmission.[463] We therefore have interpreted the case law in light of changed circumstances and have relied in the first instance on the plain wording of the statute. We find compelling that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce without qualification; unlike our jurisdiction over sales of electric energy, which section 201 specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission.

Since the time Order No. 888 issued, the D.C. Circuit has addressed a similar issue in interpreting section 1(b) of the NGA, the provision that parallels section 201(b) of the FPA. Under section 1(b), the Commission's jurisdiction does not apply "to the local distribution of natural gas or to the facilities used for such distribution." Similarly, under section 201(b) of the FPA, the Commission shall not have jurisdiction, except as specifically provided, "over facilities used for the generation of electric energy or over facilities used in local distribution ..." In responding to arguments regarding the scope of state authority

---

[463] On rehearing, several parties argue that at least one court case, *Wisconsin-Michigan Power Co. v. FPC*, 197 F.2d 472 (7th Cir. 1952), *cert denied*, 345 U.S. 934 (1953) explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services. The Commission discussed this case in detail in appendix G to the Final Rule. *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,974-75; *mimeo* at pp. 22-25. As we stated there, the court's interpretation of the legislative history of the FPA was at odds with both the plain words of the statute as well as the language of the House Report on the FPA (H.R. Rep. No. 1318 at p. 27). It also did not mention the Senate Report on the FPA, which clearly recognized jurisdiction over all interstate transmission lines, whether or not a sale of energy is carried by those lines (S. Rep. No. 621 at p. 48). We therefore reject arguments that this single case is in any way dispositive of the issue before us.

over "local distribution" of natural gas, the court distinguished between bundled and unbundled sales:

> States have been—and are still—permitted to regulate LDC's bundled sales of natural gas to end-users because those transactions include transportation over local mains and the retail sales of gas. In contrast, states have *never* regulated the terms and conditions of interstate pipeline transportation. When the gas sales element is severed—i.e., unbundled—from the transactions, FERC retains jurisdiction over the *interstate transportation* component." *(United Distribution Companies*, 88 F.3d at 1153 (footnote omitted) (emphasis in original).)

The court's reasoning is also applicable to and supports our jurisdictional determination in Order No. 888.

Several state commissions point to section 212(h) of the FPA and argue that Congress in refusing to grant the Commission authority over retail wheeling, left all jurisdiction over retail transmission to the states. We disagree. What Congress did in section 212(h) was to prohibit us from *ordering* transmission directly to an ultimate consumer. We readily recognize and respect this prohibitation. However, the ability to order retail wheeling is a separate issue from whether we have jurisdiction over the rates, terms and conditions of retail wheeling in interstate commerce that is ordered by a state or that is provided voluntarily. Congress, in enacting section 212(h), did nothing to modify our jurisdiction under sections 201, 205 and 206 over the rates, terms and conditions of interstate transmission by public utilities.

Similarly, we reject FL Com's arguments that section 212(g) of the FPA prohibits the Commission from asserting any jurisdiction over unbundled retail transmission. Section 212(g) prohibits the Commission from issuing an order that is

inconsistent with any state law that governs retail marketing areas of electric utilities. As we stated in the Final Rule, while our jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. We also reject arguments by the FL Com that this Commission's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. This argument is flatly contrary to the longstanding interpretation of the FPA by the United States Supreme Court.[464]

Commission's Seven Factor Test

IL Com argues that the Commission should withdraw its technical test. It contends that retail wheeling jurisdiction should follow function and that the function served by public utility facilities in providing retail service does not change upon the unbundling of service to retail customers. According to IL Com, Commission jurisdiction would extend to the service of delivering electric energy by a public utility to wholesale customers, regardless of the nature and extent of the public utility's facilities used to make that delivery. Similarly, it asserts state jurisdiction would extend to the service of delivering electric energy by a public utility directly to retail customers, regardless of the nature and extent of the public utility's facilities used to make that delivery.

---

[464] *See FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964) (Colton case). IN Com makes a similar argument and opposes "federalization" of retail wheeling within a state's boundaries. We reject this argument on the same basis.

NARUC argues that the seven-factor test does not result in the bright line discussed in *FPC v. Southern California Edison Company*, 376 U.S. 205 (1964). The facility-by-facility categorization of utility systems on a company-specific basis, it asserts, is hardly consistent with the Court's decision to make case-by-case analysis unnecessary.

OH Com asserts that the seven factors provide no useful insight into the nature of local distribution service. It adds that reliance upon technical tests to determine local distribution lacks legal foundation. It further contends that the jurisdictional bright line established by Congress focuses upon the nature of the transaction, not the functional or technical characteristics of a particular wire, in determining whose jurisdictional authority attaches to a particular transaction and facilities. It concludes that the Commission should adopt the Ohio-proposed retail marketing area, "wheeling in" jurisdictional approach.

PA Com contends that the Commission's seven indicia are not acceptable measures of local distribution and challenges each factor.

NH & MI Coms declare that the criteria for distinguishing transmission facilities from local distribution facilities should not be limited to the seven given in the Rule, but should allow consideration of any other relevant criteria for separating local concerns from matters legitimately federal in nature.

NJ BPU argues that the engineering-driven definition does not resolve many of the hazy areas. To the extent that the seven factors do not reflect or cannot be reconciled with the particular circumstances, it contends that the states may be hamstrung in

their ability to make reasoned decisions that comport with Order No. 888.[465]

Similarly, NY Com argues that five of the seven factors (1, 2, 4, 6, and 7) are not accurate when applied to large metropolitan areas and remote rural areas. It asserts that local distribution facilities are not necessarily close to retail customers and the assumption that local distribution facilities are primarily radial in character fails to account for network systems. It adds that reconsignment or transportation of power to different markets can and does occur at the local distribution level. It further adds that the presence of meters is not a discerning characteristic of where interstate transmission ends and local distribution begins; meters are frequently not part of the transmission/local distribution interface. Nor, according to NY Com, are local distribution systems necessarily of reduced voltage. Instead of the 7 criteria, NY Com argues that the Commission should adopt a functional measure of local distribution based on factors 3 and 5 (interstate transmission ends and local distribution begins where electricity flows into a comparatively restricted geographic area and does not flow back out of that area and the power is consumed in that area) and on the traditional classification of the facilities by the state regulatory body (or what the utility has traditionally classified as local distribution).

Commission Conclusion

Several parties on rehearing do not like the seven-factor technical test for local distribution facilities that was set forth in Order No. 888. That test takes into account both technical and

---

[465] *See also* WI Com (criteria do not appropriately reflect the mixed nature of many facilities in systems that are closely integrated and the application of the criteria to the electric system in Wisconsin would supplant state jurisdiction over a large number of facilities whose primary functions are local reliability and retail service).

functional characteristics of the transaction involved. The parties on rehearing propose instead a variety of bright line tests. For example, IL Com wants state jurisdiction to extend to the "service" of delivering electric energy to retail customers, which it would define to give it jurisdiction regardless of the nature and extent of the facilities used to make the delivery. OH Com proposes that the Commission adopt a retail marketing area "wheeling in" jurisdictional approach which would give it jurisdiction over facilities within territorial boundaries.

In response, we do not interpret the FPA to permit us in effect to rewrite the statute to give states jurisdiction over interstate transmission services. Moreover, we reject arguments of OH Com that our seven-factor test lacks legal foundation, and arguments of NARUC that we are somehow bound to develop a bright line test. While Congress established a jurisdictional bright line between wholesale and retail sales of energy, there is no such bright line that we can divine with regard to transmission and local distribution facilities. The Supreme Court, in both *Colton* and *CL&P*,[466] has instructed us that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. The seven factors will permit us to undertake this fact-specific determination.

We acknowledge the concerns raised by several state commissions that the seven-factor test does not, as NJ BPU puts it, resolve many of the hazy areas, and that there may be other factors that should be taken into account in particular situations. The seven-factor test is intended to provide sufficient flexibility to take into account unique local characteristics and historical usage of facilities used to serve retail customers. We specifically stated in the Final Rule that we will consider jurisdictional recommendations by states that take into account other technical

[466] *See Colton*, 376 U.S. at 210 n.6: CL&P, 324 U.S. at 531-36.

factors that states believe are appropriate in light of historical uses of particular facilities. Moreover, we will defer to facility classifications and/or cost allocations that are supported by state regulatory authorities. For example, in the ongoing California electric utility restructuring proceeding, the Commission deferred to the State PUC's recommendations regarding the split between state jurisdictional local distribution facilities and Commission-jurisdictional transmission facilities.[467]

Oppose transmission of public utility purchases for sale at retail

IL Com objects to the transmission unbundling requirement if it is intended to require public utilities to take transmission services under their own FERC tariffs for purchases of power intended for distribution by the public utility to retail customers. According to IL Com, a distinction must be made between the public utility's use of its transmission system in cases in which the public utility purchases wholesale power for sale for resale, and cases in which the public utility purchases wholesale power to serve native load retail customers. It argues that the Commission cannot legally regulate, or place conditions on, the manner in which a utility uses its transmission system to make sales of electric energy at retail. It contends that the Commission must exempt public utility power purchases for sale at retail from the unbundling requirement. It recommends that the Commission insert the words "for sale for resale" after the word "purchases" in section 35.28(c)(2) and after the word "purchase" in section 35.28(c)(2)(i).

[467] *Pacific Gas and Electric Company, et al.*, 77 FERC ¶61,325, at p. 61,325 (1996).

Commission Conclusion

The Commission rejects arguments of IL Com that if unbundled retail wheeling occurs either voluntarily or as a result of a state retail program, we cannot require the utility to take service under its own transmission tariff for sales to retail customers. This requirement is a term and condition of unbundled retail interstate transmission service and, as explained above, therefore is within our exclusive jurisdiction. Additionally, this should not in any way infringe on state retail programs or service to retail customers. Rather, it ensures that non-discriminatory transmission services are provided to all potential retail power competitors.

Further, as stated previously in section IV.C.1.b (Transmission Providers Taking Service Under Their Tariff), we clarify that a transmission provider does not have to "take service" under its own tariff for the transmission of power that is purchased on behalf of bundled retail customers.

Oppose buy-sell transaction analysis

PA Com asserts that there is a potential for jurisdictional conflict with respect to buy-sell transactions that is a direct consequence of the technical-functional test (which PA Com challenges).

IL Com argues that states have exclusive authority to regulate buy-sell arrangements as bundled retail sales. It further argues that the Commission cannot make a bundled retail sale into an unbundled retail sale simply by characterizing it as the functional equivalent of an unbundled retail sale; by re-characterizing them the Commission is effectively ordering the unbundling of buy-sell arrangements. It asserts that buy-sell arrangements on the electric side are not an end run around clear federal jurisdiction and that the Commission should withdraw its assertion of

jurisdiction over the retail transmission component of unbundled retail sales.

VT DPS contends that the Commission's rationale is flawed. "FERC's analysis rests on the same very shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies."According to VT DPS, all retail transactions are subject to state jurisdiction and asks the Commission to clarify that the Commission defines buy-sell as it did in the NOPR, but also acknowledge that it has no jurisdiction over such arrangements.

IN Com asserts that in the absence of any record of abusive and undermining actions by states under the guise of buy-sell arrangements, there is not even a remedial justification to touch buy-sell transactions. It contends that a difference between the FPA and the NGA warrants different treatment—the FPA exempts from FERC jurisdiction local distribution and transmission of electric energy in intrastate commerce. By redefining interstate transmission, INC Com claims that the Commission proposes to do away with the meaning history has accorded to a variety of transactions previously considered wholly intrastate in nature. According to IN Com, states should be allowed to experiment with and allow different forms of buy-sell transactions as part of the evolving marketplace.

Commission Conclusion

Four parties (PA Com, IL Com, VT DPS and IN Com) have raised concerns regarding the Commission's determination that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third party. The Commission reiterates that we will have to address these situations on a case-by-case basis. We disagree with IL Com that States have exclusive authority to regulate the interstate transmission component of buy-sell

transactions. Similarly, we deny the VT DPS request that we acknowledge no jurisdiction over such arrangements. The fact remains that these arrangements could be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. We reserve our authorities to ensure that public utilities and their customers are not able to circumvent non-discriminatory transmission in interstate commerce. In response to VT DPS' contention that the Commission's analysis here rests on the same shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies, we note that the D.C. Circuit recently affirmed the Commission's assertion of jurisdiction over buy/sell arrangements under the Natural Gas Act.[468]

State jurisdiction over the service of delivering electric energy to end users

Rehearing Requests

IL Com states that it is far from clear what FERC contemplates by the "service" of delivery of electric energy by a delivering utility in the retail wheeling transaction. It is equally unclear to IL Com whether the "service" to which Order No. 888 refers is a public utility activity over which state regulators would have jurisdiction. IL Com argues that it is the Illinois legislature, not FERC, that determines whether IL Com can regulate something called "delivery service."[469]

---

[468] *United Distribution Companies*, 88 F.3d at 1154-57.

[469] *See also* AK Com (should not create a fictional concept of delivery service—the legal reality is that, under retail competition, state law will establish a customer's right to be served and a generation owner's right to produce power. AK Com asserts that the state can then attach conditions to those rights).

MO/KS Coms ask the Commission to clarify the meaning of the statement that even when the test for local distribution facilities identifies no local distribution facilities, the Commission believes that states have authority over the service of delivering electric energy to end users. According to MO/KS Coms:

> "The authority to shop at retail and to sell at retail do not exist in the FPA. If the Commission's goal is to recognize the States' authority to establish conditions on retail competition, it need only acknowledge the State jurisdiction to establish the opportunity to shop and sell at retail. If this is what the Commission is seeking to accomplish by its discussion of 'delivery service' then we support the Commission."[470]

Coalition for Economic Competition asserts that the Commission failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, and that the local regulatory commission may have no jurisdiction over either the sale or the transmission of the energy.

Commission Conclusion

Several parties ask us to clarify our conclusion that even when the seven-factor test for local distribution facilities does not identify local distribution facilities, we believe states have authority over the "service" of delivering electric energy to end users. We clarify that states have the authority to determine the retail marketing areas of electric utilities within their jurisdictions, and the end user services that those utilities must provide, but we did not in Order No. 888 intend to opine on the extent of authority given by state legislatures to their state commissions. Rather, our statement regarding state authority

---

[470] MO/KS Coms at pp. 1-13.

over the "service" of delivering electric energy is intended to recognize the historical and local nature of delivering power to end users and the states' legitimate concerns and responsibilities in regulating local matters.

Deference to states

Rehearing Requests

Support broader deference

NARUC and IL Com argue that the Commission should not simply defer to state recommendations concerning the application of the seven-factor test or the recovery of stranded costs, but should conclusively rely on the findings by state commissions.

NY Com argues that the Commission should not limit deference to instances in which states order retail wheeling, but should defer to all state commission recommendations regarding the definition of local distribution facilities.

FL Com asserts that the Rule fails to , where deference will be given. It argues that the Rule shou. state that when a state commission has held a proceeding on matters related to the requirements of the Rule, the Commission shall give deference to the state commission decisions. Moreover, it asserts that the Commission should codify the deference stranded: "When a state commission has held a proceeding on matters related to the requirements of this rule, the Commission shall give deference to the state commission decisions." (FL Com at pp. 7-9).

The commitment to defer to a state regulatory commission or agency, argues NE Public Power District, should be clarified with respect to utilities located in Nebraska, which has no such commission or agency. NE Public Power District assumes that

deference will be accorded to decisions of NE Public Power District's Board of Directors; if not, it asks the Commission to clarify.

PA Com asks the Commission to clarify what a state regulatory agency must demonstrate to secure deference and to define the term "consult." PA Com states that, in discussing the seven indicia, the Commission states that it will "consider" jurisdictional recommendations by states, which PA Com asserts is much different from deference. It also asserts that the Commission must clarify what it will do if a utility's classifications and/or cost allocations are not supported by state regulatory authorities.

Oppose deference to state authorities

TANC argues that the Commission erred in deferring to state regulatory authorities in drawing jurisdictional lines for local distribution facility classifications and/or cost allocations. According to TANC, the Commission unlawfully and unnecessarily abdicated its jurisdiction under the FPA (citing *New England Power Co. v. New Hampshire*, 455 U.S. 331, and *Nantahala Power and Light Co. v. Thornburg*, 476 U.S. 953). With respect to ISOs, it asserts that the Commission should not defer to state authority in making determinations with respect to classifications of facilities.

Commission Conclusion

In response to NARUC an IL Com's arguments that this Commission should not simply defer to state commissions regarding application of the seven-factor test but instead should conclusively rely on the findings of state commissions, we believe this is inconsistent with the case law which states that local distribution is a matter of fact for the Commission to

determine as an original matter.[471] Additionally, we have an independent obligation to ensure that we are fulfilling our responsibilities under the FPA to regulate facilities that are used in interstate commerce. We cannot delegate our jurisdiction. However, we intend to provide broad deference to states in determining what facilities are Commission-jurisdictional transmission facilities and what facilities are state-jurisdictional local distribution facilities, so long as our comparability principles are not compromised and we are able to fulfill our responsibilities under the statute.

We reject FL Com's suggestion that we codify the deference standard. This is neither necessary nor appropriate. In response to NE Public Power District's request that we clarify to whom we would give deference in Nebraska, we clarify that because Nebraska does not have an electric regulatory commission or agency, there is no appropriate regulatory entity to whom our deference standard would apply; accordingly, we will address the transmission/local distribution issue for Nebraska without giving deference to any particular entity. In response to PA Com's request that we clarify what we will do if a utility's classifications and/or cost allocation proposals are not supported by state regulatory authorities, we will make a determination based on the factual record before us in a particular case, taking into account the views of the state regulatory authority.

TANC has argued that we have unlawfully abdicated our jurisdiction by deferring to state recommendations. TANC confuses delegation of jurisdiction, which we cannot do with willingness to defer to states based on their application of criteria that we have provided. Even in the cases in which the Commission defers to states' views, we will still independently evaluate all material issues and proceed only where substantial

---

[471] *See Colton* and *Connecticut Light and Power, supra.*

evidence supports the states' views. The Commission clearly can entertain requests for deference in these circumstances.

J. *Stranded Costs*

As indicated in our prior discussion in Section IV.A.5. there are two major overlapping transition issues that arise as a result of this rulemaking: stranded cost recovery and how to deal with contracts entered into under the prior regulatory regime. We here address stranded cost recovery and, as in the prior discussion, we believe it is important to explain the general context in which our stranded cost determinations have been made before addressing the various rehearing requests on this issue.

In Order No. 888, the Commission removed the single largest barrier to the development of competitive wholesale power markets by requiring non-discriminatory open-access transmission as a remedy for undue discrimination. This action carries with it the regulatory public interest responsibility to address the difficult transition issues that arise in moving from a monopoly, cost-based electric utility industry to an industry that is driven by competition among wholesale power suppliers and increasing reliance on market-based generation rates. The most critical transition issue that arises as a result of the Commission's actions in this rulemaking is how to deal with the uneconomic sunk costs that utilities prudently incurred under an industry regime that rested on a regulatory framework and a set of expectations that are being fundamentally altered.

The Commission determined in Order No. 888 that it must address stranded costs, and that it must do so at an early stage—particularly in light of the lessons learned from our experience with similar issues in the natural gas area. We noted that when we did a similar restructuring in the gas industry, the D.C. Circuit invalidated the Commission's efforts precisely

because the Commission had failed to deal with the stranded cost problem in a satisfactory manner.[472] We explained that, based on the lesson of AGD, the Commission cannot change the rules of the game without providing a mechanism for recovery of the costs caused by such regulatory-mandated change.

Since the time Order No. 888 issued, we have been provided with additional guidance from the court in the natural gas area, which has further helped to inform our decisions here. In its decision on review of Order No. 636,[473] the D.C. Circuit upheld the Commission's decision to allow the recovery of gas supply realignment costs. In so doing, the court, while questioning a specific feature of the stranded cost recovery mechanism employed in Order No. 636, has nevertheless again reaffirmed the basic principle that stranded cost recovery is an appropriate component of a regulatory policy aimed at accomplishing a fair and reasonable transition to competitive markets. The question as to the Commission's ability to allow the recovery of stranded costs has been laid to rest.

The task before the Commission in this rulemaking is thus to determine how best to meet its responsibility to address the costs of the transition to a competitive industry, particularly insofar as those costs are stranded, or in effect rendered unrecoverable, as a result of the transmission access required by us under the FPA.[474] As the rehearing arguments demonstrate, there is no consensus on how the Commission should address the stranded cost issue. In fact, petitioners are at polar extremes as to what

---

[472] *Associated Gas Distributors v. FERC*, 824 2d 981 (D.C. Cir. 1987). *cert. denied.*, 485 U.S. 1006 (1988) (AGD).

[473] *United Distribution Companies v. FERC*, 88 F.3d 1105 (1996) (*United Distribution Companies*).

[474] Such access may be the open access required under this rule or case-by-case transmission access ordered pursuant to FPA section 211.

the Commission should do regarding stranded costs. Some argue that the Commission has gone too far in permitting utilities to seek recovery of stranded costs, whether such costs are associated with wholesale requirements contracts, with retail-turned-wholesale customers, or with retail customers that obtain retail wheeling.[475] Others argue that the Commission has not gone far enough and that it must broaden the scope of stranded cost recovery permitted under the Rule. Indeed, some would have us be the guarantor for recovery of all uneconomic costs that might be stranded in the move to more competitive markets, no matter how tenuous the nexus to this Rule, and irrespective of state-Federal jurisdictional complexities. Some support the Commission's decision to recover stranded costs directly from the departing customers. Others would prefer that the Commission require utilities to absorb a portion of their stranded costs or that the Commission spread the burden of stranded costs among all of the utility's customers. Some object that the Commission's approach to stranded costs in the electric industry is different from that adopted in the gas industry. Some entities support the Commission's revenues lost approach for measuring a departing customer's stranded cost obligation. Others propose different methods for computing stranded costs.

Given the plethora of positions that entities have raised both initially and on rehearing concerning stranded costs, the

---

[475] We note that the regulations implementing this rule use "wholesale stranded cost" and "retail stranded cost" as shorthand terms to refer to the different situations in which a utility may experience stranded costs. However, as the definitions of those terms make clear, it is *not* the nature of the *costs* (wholesale vs. retail) that is controlling for purposes of stranded cost recovery under this Rule. Rather, the controlling factors are the status of the *customer* (wholesale transmission services customer vs. retail transmission services customer) with whom the costs are associated, and whether the transmission tariffs used by the customer to escape its former power supplier (thus causing the stranding of costs to occur) were required by this Commission or by a state commission. As a result, "retail stranded costs" refers to stranded costs associated with retail wheeling customers.

Commission has taken a careful, measured approach with regard to stranded cost recovery. The Commission has balanced a number of important interests in order to achieve what it believes will be fair and orderly transition to competitive markets. These interests include the financial stability of the electric utility industry, upholding the regulatory bargain under which utilities made major capital investments, and not shifting costs to customers that had no responsibility for causing those costs to be incurred. The Commission also has adopted an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of stranded cost recovery from retail customers, recognizes state commission jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures.

The balancing of interests and considerations described above is reflected in the following central components of the Rule's stranded cost provisions, which are reaffirmed herein.[476] First, the Commission has determined that the most reasonable, legally supportable approach is one that permits utilities to seek recovery of wholesale stranded costs under this Rule (whether the stranded costs are associated with a departing wholesale requirements customer or with a retail-turned-wholesale customer) only in those cases in which there is a *direct nexus* between the availability and use of Commission-required transmission access[477] and the stranding of costs. In order for the

[476] We reaffirm below our basic determinations, but make certain clarifications on limited issues, and grant rehearing on the municipal annexation issue.

[477] As we explain below, by "Commission-required transmission access" we mean the open-access transmission required under this rule or required pursuant to a section 211 order, as well as transmission provided prior to Order No. 888 (and not pursuant to a section 211 order) where such

utility to be eligible to seek recovery of stranded costs from a departing customer, the customer must have obtained access to a new generation supplier through the use of the former supplying utility's Commission-required transmission tariff (i.e., its open-access tariff or a tariff ordered pursuant to FPA section 211), not through the use of another utility's transmission system.

Other cost recovery issues are more appropriately addressed outside the context of this Rule. For example, the Rule is *not* intended to apply to costs associated with the normal risks of competition, such as self-generation, cogeneration, or loss of load, that do not arise from the new, accelerated availability of Commission-required transmission access. If a customer leaves its utility supplier by exercising options that could have been undertaken prior to mandatory transmission under Order No. 888 or the Energy Policy Act, or that do not rely on access to the former seller's transmission, there is no direct nexus to Commission-required transmission access and thus no opportunity for stranded cost recovery under the Rule.

Second, the Commission has limited the opportunity to seek stranded cost recovery under the Rule primarily to two discrete situations: (1) costs associated with customers under wholesale requirements contracts executed on or before July 11, 1994 (referred to in the Rule as "existing wholesale requirements contracts") that do not contain an exit fee or other explicit stranded cost provision; and (2) costs associated with retail-turned-wholesale customers. With regard to the existing wholesale requirements contracts, the Commission also has made a finding that it is in the public interest to permit amendments to add stranded cost provisions to these contracts, even if they

transmission was provided on a case-by-case basis to comply with the Commission's comparability requirement. *See* note 484 *infra*.

contain *Mobile-Sierra* clauses, if case-by-case evidentiary burdens are met. We do not interpret the *Mobile-Sierra* public interest standard as practically insurmountable in extraordinary situations such as this one where historic statutory and regulatory changes have converged to fundamentally change the obligations of utilities and the markets in which they and their customers will operate.

Third, Order No. 888 *does not guarantee* that a utility will be allowed to recover stranded costs. Rather, it provides an *opportunity* for such recovery. To be eligible to recover stranded costs from a departing customer in a particular case, the utility must demonstrate that it incurred costs to provide service to the customer based on a reasonable expectation of continuing service to that customer beyond the contract term.[478] In the case of stranded costs associated with wholesale requirements contracts customers, if the contract contains a notice of termination provision, that provision is strong evidence that the parties were aware that at some point in the future the customer might seek to find another supplier. Therefore, there is a rebuttable presumption of no reasonable expectation, and therefore no opportunity for stranded cost recovery unless the utility can overcome the presumption.

The Commission has concluded that direct assignment of stranded costs to the departing customer (through either an exit fee or a surcharge on transmission) is the appropriate method for recovery of stranded costs under the Rule. In reaching this conclusion, the Commission carefully weighed the arguments supporting direct assignment of stranded costs against those supporting a more broad-based approach, such as spreading

---

[478] We have made a minor revision to the regulatory text, section 35.26(c)(2), to conform the language of that section with sections 35.26(b)(1) and (5). A conforming revision has been made to section 35.26(d)(2)(i).

stranded costs to all transmission users of a utility's system, and also took into account the fact that we applied a different approach in the natural gas area. The central considerations that support a direct assignment approach in the electric industry are that the approach follows the traditional regulatory concept of cost causation, it avoids shifting costs to customers that had no responsibility for causing them to be incurred or for causing them to be stranded, and it is still possible to apply such an approach at this stage of the industry's evolution.

There is no question that, without the stranded cost recovery mechanism, some customers would be far more likely to switch to lower-cost suppliers and enjoy sooner the benefits of a competitive power market. But, as detailed in Order No. 888, such an approach may result in higher costs for other customers. We thus have had to balance the potential for earlier benefits for some customers against other public interest considerations, most particularly the need to provide a fair mechanism by which utilities can recover the costs of past investments under traditional regulatory concepts of prudently incurred costs and cost causation. The result is not to deny competitive advantages, but only to delay their full realization for some customers so that all customers ultimately will benefit.

While Order No. 888s cost causation approach is different from the Order No. 636 cost spreading approach that was affirmed in the *United Distribution Companies* case, we believe it is the preferable approach given the early stage of the electric utility's competitive transition. We do not read the court's opinion as precluding the Commission from adopting a direct assignment approach in Order No. 888, particularly where, as here, the Commission has fully explained and justified the reasons for following traditional cost causation principles. In addition, although the *United Distribution Companies* court remanded for further consideration (in light of Order No. 636's cost spreading approach) the decision not to require any pipeline

absorption of gas supply realignment costs, the Commission has fully explained how its decision in Order No. 888 not to require any utility absorption of stranded costs is consistent with its decision to follow traditional cost causation principles. With respect to the fundamental conclusion that utilities should be permitted an opportunity to recover their prudently incurred costs, Order No. 888 is fully consistent with Order No. 636. Although the Commission in Order No. 888 chose a direct assignment method (rather than the cost-spreading approach in Order No. 636) for purposes of allocating stranded cost responsibility among customers, the approach used by the Commission in Order No. 888 is not governed by decisions in Order No. 636, but in either event the Commission must demonstrate that its choice of methods is based on reasoned decision-making.

In considering the stranded cost issues that may arise in the transition to competitive markets, the Commission also has taken cognizance of significant changes involving retail customers and the stranded cost issues that arise as retail customers convert to wholesale customer status (e.g., through municipalizations) in order to obtain the open access afforded by Order No. 888, or as they obtain retail wheeling required by state commissions. These situations involve new and complex jurisdictional issues and represent the bulk of potential stranded costs facing the industry. We believe it is important to clarify the Commissions' decisions as to when it will entertain requests for stranded cost recovery in these situations, and our reasons for doing so.

The Commission's determination that it, rather than the states, should be the primary forum for addressing stranded costs associated with a retail-turned-wholesale customer[479] is limited

[479] In Order No. 888 and here, we sometimes use the shorthand expression "retail-turned-wholesale" customer. By this we do not mean that a retail customer who is an ultimate consumer ceases to be an ultimate consumer, or that this customer begins to purchase electric energy for resale. Rather, in a "retail-turned-wholesale customer" situation, such as the creation of a municipal utility system, a newly created entity becomes a wholesale power purchaser on behalf of retail customers who were formerly bundled customers of a the historical local utility power supplier. The new municipal utility is the conduit by which retail customers, if they cannot obtain direct retail access, can reach power suppliers other than their historical local utility power supplier. Although the retail customers remain bundled retail customers, in that they become the bundled customers of the new entity, we call this a "retail-turned-wholesale customer" situation because the new entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply.

to those cases in which there is a *direct nexus* between the availability and use of Commission-required transmission access and the stranding of costs. We believe we have both the authority and the obligation to provide an opportunity for stranded cost recovery in these situations because the bundled retail customer would not be able to obtain access to the new supplier *but for* the Commission's order requiring transmission. The creation of a new wholesale entity to purchase power on behalf of retail customers would not, by itself, trigger stranded costs. In the absence of transmission access from the historical supplier of the retail customers, the new entity would have to remain on the historical supplier's generation system because it would have no way to reach other power suppliers, and stranded costs would not occur.[480] Therefore, there is a casual nexus between the stranded costs and the availability and use of the

[480] Exceptions would be self-generation or construction by the new entity of its own transmission line, in which case, as noted earlier, the stranded cost provisions of Order No. 888 would not apply because such option have always been available as alternatives to purchasing power from the historical supplying utility and do not involve the use of the utility's transmission facilities under an open-access tariff. Thus the departure of customers under these circumstances cannot be linked to the open-access requirements of this Rule.

tariff services *required by the Commission*.[481] Moreover, because of this casual nexus between the use of a jurisdictional utility's Commission-required transmission tariff and the potential for foregone revenues by that jurisdictional utility as a result of the Commission-required access, the stranded costs associated with a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In contrast, in the situation in which a bundled retail customer obtains retail wheeling, stranded costs are directly caused by the availability and use of unbundled retail services *required by the state commission*, not this Commission.[482] Thus, the Commission believes that states, not the Commission, should be the primary forum for costs associated with a bundled retail customer that obtains retail wheeling. The Commission's decision to entertain request to recover stranded costs caused by retail wheeling in *only* a limited circumstance (where the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on a policy decision by this Commission that it will step in to fill a regulatory "gap" that could result in no effective forum in which utilities would have an opportunity to seek recovery of prudently incurred costs.

---

[481] As discussed in greater detail in sections IV.J.6 and IV J.12 below, we clarify that the opportunity for recovery of stranded costs in retail-turned-wholesale situation is limited to cases in which the former bundled retail customer subsequently becomes, either directly or through another wholesale transmission purchaser, an unbundled wholesale transmission services customer of its former supplier. We have revised section 35.26(b)(1)(i) of the Commission's regulations accordingly.

[482] Unbundled retail transmission services required by a state commission could be taken under the same *pro forma* open-access tariff used by wholesale customers or, if determined appropriate by the Commission, under a separate retail tariff filed at the Commission. The critical point, however, is that in either case, the unbundled services are required by the state and not by this Commission.

Finally, after considering various proposals regarding how stranded costs should be calculated, and reviewing the arguments of petitioners on rehearing, the Commission continues to believe that the revenues lost approach is the fairest and most efficient way to determine the amount of stranded cost assigned to a departing customer during the transition to a competitive wholesale bulk power market. The Commission has rejected an asset-by-asset approach as overly complicated and costly.

We respond below to the specific arguments raised on rehearing and elaborate on the above determinations.

1. Justification for Allowing Recovery of Stranded Costs

In Order No. 888, the Commission concluded that utilities should be given the opportunity to seek recovery of legitimate, prudent and verifiable stranded costs associated with a limited set of wholesale requirements contracts executed on or before July 11, 1994.[483] We stated that utilities that entered into contracts to make wholesale requirements sales under an entirely different regulatory regime should have an opportunity to recover stranded costs that occur as a result of customers leaving the utilities' generation systems through Commission-

* * * * *

would affect market participants unequally. Those with long terms remaining on their contracts could object that immediately addressing the issue would not be cost effective. A utility with a long remaining term might not even seek stranded cost recovery depending on the competitive value of its assets near the end of

---

[483] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,788-91; *mimeo* at pp. 451-58.

the contract term.[671] However, such a utility would invariably seek to preserve its option to seek stranded cost recovery if its failure to do so within a short period resulted in a waiver of its right to do so. Having determined that it is generally appropriate to leave in place existing requirements contracts, it is not then reasonable to create a time limitation on stranded cost recovery that would encourage a supplier to seek early termination in order to preserve its stranded cost recovery rights.

On this basis, we believe that we have adequately explained the rationale for our decision to allow stranded cost claims to be raised at any time prior to the termination of the contract, instead of within three to five years of the effective date of the Rule.

6. Recovery of Stranded Costs Caused by Retail-Turned-Wholesale Customers

In Order No. 888, we concluded that this Commission should be the primary forum for addressing the recovery of stranded costs caused by a retail-turned-wholesale customer.[672] We stated that if such a customer is able to reach a new generation supplier because of the new open access (through the use of a FERC-filed open-access transmission tariff or through transmission services ordered pursuant to section 211 of the FPA), any costs stranded as a result of this wholesale transmission access should be viewed as "wholesale stranded costs." We explained that there is a clear nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs and that, in these circumstances, this

[671] The value of its assets could vary over time as new technologies emerge, fuel costs fluctuate, or environmental requirements change.

[672] *FERC Status and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,818-19; *mimeo* at pp. 534-37.

Commission should be the primary forum for addressing recovery of such costs.[673]

We said we will not be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory. We indicated that in these situations there is no direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs. The risk of an existing municipal utility expanding its territory was a risk prior to any open-access requirement.

Nevertheless, we did express concern that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open-access transmission, to circumvent the ability of any regulatory commissions—either this Commission or state commissions—to address recovery of stranded costs. We reserved the right to address such situations on a case-by-case basis.

Rehearing Requests Opposing Retail-Turned-Wholesale Jurisdiction

A number of entities challenge the Commission's assertion that costs associated with retail-turned-wholesale customers would not be stranded but for the FERC-jurisdictional transmission access requirement. They assert that the condition precedent to municipalization is the operation of a state process, and thus that it cannot be the case that the recovery of costs caused by a retail-turned-wholesale customer is "not subject to

[673] We indicated that we will require the same evidentiary demonstration for recovery of stranded costs from a retail-turned-wholesale customer (and will apply the same procedures for determining stranded cost obligation) as that required in the case of a wholesale requirements customer.

regulation by the States." They submit that such costs would not be stranded but for the action of state legislators or state regulators in granting authority for the customer's status change. They argue that any nexus that the Commission's authority under the FPA has to wholesale transmission services subsequently provided to the new wholesale customer is entirely derivative of the state's action.[674]

A number of entitles argue that jurisdiction over costs that are stranded when a retail customer becomes a wholesale customer should be left to the states because the facilities used to provide retail service to these retail customers were subject to state jurisdiction and were included in retail rate base when the service was rendered.[675] They argue that because the Commission had no jurisdiction over the public utility facilities and costs incurred to serve retail-turned-wholesale customers, it has no jurisdiction to address those public utility costs if they become stranded. Thus, according to these entities, the conversion of the customer from retail to wholesale does not simultaneously effectuate a conversion of the costs from retail to wholesale.

AR Com and MO/KS Coms submit that jurisdiction over the costs incurred for historical retail customers does not shift unless the parties themselves make those costs a part of their new wholesale contract. NY Com submits that the Commission should recognize the states' jurisdiction to set the level of stranded costs associated with retail-turned-wholesale customers to be recovered in wholesale transmission rates set by FERC. FL Com asserts that state authorities are in a better position to

---

[674] *E.G.*, NARUC, TAPS, Nucor, Suffolk County, IL Com, Multiple Intervenors, APPA, CAMU, WI Com, NASUCA.

[675] *E.g.*, ELCON, IL Com, IN Com, American Forest & Paper, AR Com, MO/KS Coms, NJ BPU, Suffolk County, WY Com, VA Com, FL Com, NARUC, TAPS.

assess the extent of stranded facilities and their costs, and that the Commission's involvement should be limited to that requested by a state by petition.

OH Com states that the Commission's position on stranded costs associated with retail-turned-wholesale customers invites second-guessing of state commission determinations and encourages forum shopping by introducing more than one stranded cost treatment within a single state jurisdiction. It expresses concern that utilities may seek to creatively disaggregate into generation, transmission, and distribution companies in ways to deliberately recast traditional retail relationships as wholesale in an effort to obtain favorable regulatory treatment of stranded costs.

IN Com submits that Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers will discourage state legislatures from making municipalization more available. VT DPS and Valero argue that the threat of a stranded cost surcharge will erect a new barrier to the formation of municipal utilities. They note that the rule refers to one commenter's observation that, if Otter Tail could have made a stranded cost claim against the municipal utility that Elbow Lake planned to create, Otter Tail would not have needed to refuse to wheel and there would never have been an *Otter Tail case*. They submit that the Commission never addressed whether, or why, it believed the point to be wrong.

VT DPS and Valero also assert that the rule represents a major inconsistency with prior Commission treatment of municipalization. They submit that the Commission historically promoted franchise competition between municipalities and

utilities by holding tariff provisions that restrict such competition to be anticompetitive and unreasonable.[676]

American Forest & Paper submits that recover of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's actions in the natural gas industry, where the Commission has encouraged competition at the retail level through competitive bypass and has not created barriers to competitive entry by imposing transition charges or exit fees on converting customers.[677]

Nucor objects that the rule does not address the substantive findings, the common sense rationale, or the jurisdictional distinction drawn in *United Illuminating*.[678] It contends that the Commission's observation in Order No. 888 that there may not be a state regulatory forum for the recovery of stranded costs associated with retail-turned-wholesale customers and hence that the Commission should be the primary forum for addressing such stranded costs is flawed because there always is a state forum to address such cost recovery (the adequacy of the relief provided is a very distinct issue) and open-access transmission does not and cannot cause retail competition to occur.[679]

---

[676] VT DPS and Valero cite in this regard *Florida Power & Light Company*, 8 FERC ¶ 61,121 (1979); *Power Authority of the State of New York v. FERC*, 743 F.2d 93 (2d Cir. 1984); *Metropolitan Transportation Authority v. FERC*, 796 F.2d 584 (2d Cir. 1986).

[677] American Forest & Paper cites in support of its position *Great Lakes Gas Transmission Limited Partnership*, 68 FERC ¶ 61,376 (1994).

[678] *United Illuminating Company*, 63 FERC ¶ 61,212, *reh'g denied*, 64 FERC ¶ 61,087 (1993) (*United Illuminating*).

[679] *See also* Suffolk County Rehearing (Commission's analysis in *United Illuminating* was correct: nothing has changed to warrant the Commission's rejection of that analysis).

Commission Conclusion

We will reject the requests for rehearing of our decision to be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers. We find the requests for rehearing on this issue unpersuasive. While it may be the case, as some entities suggest, that state action is a condition precedent to municipalization, the rehearing petitions ignore the fact that the rule covers situations in which open access is *also* a condition precedent to the municipalized customers leaving their existing supplier's system. Order No. 888 does not propose that the Commission be the primary forum for stranded cost recovery for all cases of municipalization. Instead, our holding is limited to those cases in which the new wholesale entity uses Commission-mandated transmission access to obtain new power supply on behalf of retail customers that were formerly supplied power by the utility providing the transmission service.[680]

As we explained in Order No. 888, in such cases there is a direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of costs stranded as a result of this wholesale transmission access. Thus, the stranded costs associated with retail-turned-wholesale customers for which Order No. 888 provides an opportunity for recovery would not have been incurred but for the action of this Commission in requiring a utility to make unbundled transmission services available. In these cases, the former bundled retail customers of the historical supplying utility (now the bundled retail customers of the new municipal system) would

---

[680] In the case of municipalization, the bundled retail customers of a local utility become the bundled retail customers of the new municipal utility. As explained above, we call this a "retail-turned-wholesale customer" situation because the new municipal entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply.

not have obtained access to new power supply but for the Commission's order mandating transmission. Without the regulatory mandate to provide access, the utility would have indirectly continued sales to the same retail customers because the new municipal utility purchasing power on the retail customers' behalf would have had no way to reach other power suppliers. In this situation, there would be no stranded generation costs. In other words, the creation of a municipal utility intermediary to purchase power at wholesale would not, by itself, trigger stranded costs. Rather, it is the access from the historical supplier of the bundled retail customers that is the condition precedent to reaching other power suppliers and thereby triggering stranded costs. Therefore, there is a clear causal nexus between the stranded costs and the availability and use of the tariff *required by the Commission.*

Costs that are exposed to nonrecovery when a retail customer or a newly-created wholesale power sales customer ceases to purchase power from the utility and *does not* use the utility's transmission system to reach a new generation supplier (e.g., through self-generation or use of another utility's transmission system) do not meet the definition of "wholesale stranded costs" for which the rule provides an opportunity for recovery. Such costs are outside the scope of the rule because such costs would not be stranded as a direct result of the new open access.

In response to the argument that conversion of a customer from retail to wholesale would not simultaneously effectuate a conversion of the costs from retail to wholesale, we believe this argument confuses the issue. We note that we have defined stranded costs as wholesale or retail on the basis of whether wholesale or retail open access is the cause of the costs being stranded, not on the basis of the original retail or wholesale characteristic of the costs. Thus, even though costs may have been originally incurred as retail-related costs, the precipitating event that results in such costs being stranded in the retail-

turned-wholesale customer scenario is the use by the new wholesale customer of the Commission-mandated tariff. When a customer is able to use the Commission-required tariff to reach another generation supplier, it causes the utility to incur an economic cost in providing transmission service that is equal to the foregone revenues that the utility reasonably expected to receive under a state regulatory regime. Thus, because of the causal nexus between the use of a former supplying utility's Commission-mandated transmission tariff and the potential for foregone revenues by that utility as a result of the Commission-required access, the costs stranded by a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In response to those entities that express concern that the Commission's position on stranded costs associated with retail-turned-wholesale customers invites second-guessing of state commission determinations, we emphasize that we have assumed primary authority to address such costs only in a limited category of cases where there is a direct nexus between the availability of Commission-required open access and the stranding of costs when the former customer uses the former supplying utility's transmission system (through its open-access tariff or a section 211 order) to reach a new supplier. We indicated in Order No. 888 that if the state has permitted any recovery from departing retail-turned-wholesale customers, such amount will not be stranded for purposes of this Rule. We will deduct that amount from the costs for which the utility will be allowed to seek recovery under this rule from the Commission. In so doing, however, we are not second-guessing the states as to what a utility may recover under state law. Additionally, we will give great weight in our proceedings to a state's view of what might be recoverable.

We also reject the argument that the Commission's position on stranded costs associated with retail-turned-wholesale

customers encourages forum shopping. To the contrary, as we said in Order No. 888, to avoid forum shopping and duplicative litigation of the issue, we expect parties to raise claims before this Commission in the first instance. We believe that this Commission should be the primary forum because, without the open access provided by the Rule, the new municipal utility would not be able to reach a new supplier and, as a result, would not cause the utility to incur stranded costs (as defined in this Rule).

We reject as misplaced arguments that the rule represents a major inconsistency with the Commission's historical promotion of franchise competition between municipalities and utilities and that it will discourage municipalization.[681] It continues to be the Commission's policy to encourage competition. Indeed, the goal of Order No. 888 is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers. However, the purpose of the stranded cost policy is neither to encourage nor to discourage municipalization, but rather to facilitate a fair transition to competition and to ensure stability in the industry during that transition. As we discuss elsewhere in this order, we believe that this Commission must address the recovery of the costs of moving from a monopoly-regulated regime to one in which all sellers can compete on a fair basis and

[681] In response to VT DPA and Valero, we note that whether or not Otter Tail may have agreed to wheel power for the municipal utility that Elbow Lake planned to create if Otter Tail could have made a stranded cost claim against that municipal utility is of no moment to the Commission's decision in Order No. 888 to allow utilities the opportunity to seek recovery of stranded costs associated with retail-turned-wholesale customers. The Court in *Otter Trail* did not address the stranded cost issue because it was not presented in that case. Nor was the Court presented with the extraordinary circumstances—the historic statutory and regulatory changes, including the requirement of open-access, that have converged to fundamentally change the obligations of utilities and the markets in which they operate—that have justified this Commission's Order No. 888 stranded cost policy.

in which electricity is more competitively priced. On this basis, we believe that if a new wholesale entity such as a municipal utility uses Commission-required open access to reach a new supplier on behalf of its retail customers (previously retail customers of the former supplier), the former supplying utility should be given an opportunity to recover legitimate, prudent and verifiable costs that it incurred under the prior regulatory regime to serve that customer.

In response to American Forest & Paper's argument that recovery of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's policy in the natural gas industry of allowing competitive bypass without imposing transition charges or exit fees on converting customers, we note that industrial gas customers who bypass a local distribution company's (LDC) facilities do not escape transition costs quite so easily as suggested by American Forest & Paper. It is true that, when the end-user bypasses the LDC to reach an interstate pipeline different from the pipeline serving the LDC, the Commission views the bypass as a risk of competition from which the LDC should not be shielded.[682] However, when the end-user bypasses the LDC to reach the same interstate pipeline that serves the LDC, the Commission may take certain actions to minimize adverse effects on the LDC and its remaining customers.[683] Moreover, an end-user that bypasses an LDC to reach the same pipeline that serves the LDC would, in any event, be allocated a share of the pipeline's gas supply realignment costs (if any), since those costs are allocated based on current

[682] *Texas Gas Transmission Corporation*, 65 FERC ¶ 61,275 (1993).

[683] *Texas Gas Transmission Corporation*, 69 FERC ¶ 61,245, *reh'g*. 70 FERC ¶ 61,207 (1995) (requiring pipeline to offer LDC a reduction in its contract demand).

contract demand (or usage).[684] Accordingly, we see no inconsistency between our bypass policy for the natural gas industry and Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers. Similar to our refusal to shield LDCs from the adverse effects of an end-user's bypass to reach a different pipeline than serves the LDC, Order No. 888 does not provide an opportunity for stranded cost recovery where a retail-turned-wholesale customer uses another utility's transmission system to reach a new supplier. As we noted above, the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers is limited to those cases in which the former retail customer obtains (either directly or through another wholesale transmission purchaser) unbundled transmission services from its former supplying utility. In the case of an end-user customer bypassing the LDC to reach the same pipeline that serves the LDC, the end-use customer would similarly be allocated a share of the pipeline's gas supply realignment costs. As a result, American Forest & Paper's attempt to rely on the Commission's gas bypass policy is misplaced.

We also disagree with those entities that argue that the Commission has failed to adequately distinguish Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers with the Commission's decision in *United Illuminating*. As we stated in Order No. 888, we recognize that we took a different approach to stranded cost recovery associated with retail-tuned-wholesale customers in *United*

[684] *See Southern Natural Gas Company* 75 FERC ¶ 61,046, at p. 61,158 (1996); *Arcadian Corporation v. Southern Natural Gas Company*, 67 FERC ¶ 61,176, at p. 61,538 (1994). *See also United Distribution Companies*, 88 F.3d at 1181. As the *United Distribution Companies* court noted, the Commission has given an LDC relief (and required the bypassing customer to bear its share of transition costs) if the LDC can show a direct nexus between the bypass and the pipeline, although the Commission has declined to adopt a generic rule addressing this issue. 88 F.3d at 1180-81.

Illuminating, where we suggested that state and local regulatory authorities or the courts should be able to provide an adequate forum to address retail franchise matters, including recovery of stranded costs caused by municipalization, but said we would consider revisiting the question if United Illuminating could demonstrate the lack of a forum.[685] However, we explained that since the issuance of that decision we have had an opportunity to re-analyze the nature of the stranded cost problem when a retail customer becomes a wholesale customer, including the potential that there might not be a state regulatory forum for recovery of such costs. In these circumstances, we have determined that where such costs are stranded as a direct result of Commission-mandated wholesale transmission access, these costs should be viewed as costs of the transition to competitive wholesale bulk power markets and this Commission should be the primary forum for addressing their recovery.

In response to Nucor's objection that there always is a state forum to address stranded costs recovery associated with retail-turned-wholesale customers, with the adequacy of the relief being a distinct issue, we clarify that our primary concern in retain-turned-wholesale situations is not whether there is an adequate state regulatory forum for the recovery of stranded costs associated with retain-turned-wholesale customers. Rather, our primary concern is that wholesale customers (whether or not formerly retail) should be responsible for the costs incurred to meet their power needs that are stranded when they use the wholesale transmission ordered by this Commission to reach new suppliers. Our decision to be the primary forum in the case of stranded costs associated with retail-turned-wholesale customers is based on the causal nexus between regulatory-mandated wholesale transmission access and the stranding of costs when a new municipal utility uses such access to obtain new power

[685] 63 FERC at pp. 62,583-84.

supply on behalf of retail customers previously served by the former supplying utility.

Rehearing Requests Seeking Expansion of Retail-Turned-Wholesale Jurisdiction

Other entities seek rehearing of the Commission's decision not to be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory.[686] A number of them argue that the loss of existing retail customers through municipal annexations or expansions is no different from the loss of retail customers through new municipalization because existing municipal systems are likely to use Commission-jurisdictional open-access transmission to obtain resources to supply power to the annexed loads.[687] They submit that, just as with newly-municipalized customers, such costs would not be stranded but for the action of this Commission.

Some of these entities express concern that the rule will encourage retain-turned-wholesale transactions to be undertaken as annexations rather than through the formation of new entities to avoid stranded costs.[688] Public Service Co of CO contends

---

[686] *E.g.*, EEI, SoCal Edison, Centerior, Atlantic City, PSE&G, Puget, Public Service Co of CO, Coalition for Economic Compeition.

[687] *E.g.*, EEI, SoCal Edison, PSE&G, Puget, Public Service Co of CO, Coalition for Economic Competition, Coalition for Economic Competition suggests, for example, that villages and large industrial customers may opt to join existing municipal systems that, in most cases, will use Commission-jurisdictional transmission tariffs to obtain resources to supply power to the annexed loads.

[688] *E.g.*, EEI, Coalition for Economic Competition, Atlantic City, Puget, Public Service Co of CO.

that Order No. 888, in conjunction with the Commission's section 211 order in *American Municipal Power Ohio, Inc.*,[689] may facilitate municipal annexations by enabling municipal systems to serve new territory through the establishment of second delivery points.

Coalition for Economic Competition and Puget also argue that the Commission must consider stranded costs that arise from municipal expansion in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. They contend that there is no justification for charging one rate to former retail customers taking transmission services through a new municipal utility and another rate to those taking service through municipal annexation or through use of another utility's transmission system.

PSE&G suggests that the distinction between new municipalization on the one hand and municipal annexation or expansion on the other hand may lead to unnecessary controversy and litigation as entitles wrangle over whether a given expansion/annexation is really an expansion or a municipalization. It says that a situation could arise where a municipality serves one town in order to serve thousands of additional customers in a second town. According to PSE&G, it is not clear from the rule whether the Commission would consider this an expansion of a municipality's service territory or a new municipalization.

Puget submits that the stranded cost recovery mechanism must not be subject to being frustrated by simple artifices such as having the new supplier (instead of the departing customer) request and contract for transmission service. SoCal Edison

---

[689] 74 FERC ¶ 61,086, *final order directing transmission service*, 76 FERC ¶ 61,265 (1996).

seeks clarification of the Commission's authority to mandate stranded cost recovery if a retail customer disconnects from a utility's system and accesses another generation supplier by interconnecting with a public power entity (who in turn would interconnect with a neighboring jurisdictional utility). It asks the Commission to clarify that such a transaction effectively constitutes a municipalization, not an expansion of a service territory, and that the Commission, under FPA section 211, can compel the recovery of stranded costs by having the "new" jurisdictional utility assess a stranded cost charge and pass the revenues on to the utility from whose system the customer departed.

SoCal Edison seeks several additional clarifications. It states that it understands that the Commission's primary forum status in no way prevents or interferes with a state's authority to order stranded cost recovery from departing retail customers. If this is not the case, SoCal Edison seeks rehearing on this issue. SoCal Edison also seeks the Commission to clarify that the Commission retains the discretion to defer to a state stranded cost calculation methodology if appropriate to do so on the facts of a particular case.

Commission Conclusion

We have carefully reviewed the arguments made by petitioners seeking rehearing of our decision not to be the primary forum for stranded cost recovery in the case of municipal annexations. Based on that review we have decided to reconsider our decision. This conclusion is based in large part upon the very significant similarities between the creation of a *new* municipal utility system (also referred to as municipalization) and the expansion of an *existing* municipal utility system (*e.g.*, through annexation of additional retail service territory). We recognize that the same nexus to Commission-required transmission access that forms the basis for

our decision to allow a utility to seek stranded cost recovery in cases of new municipalization—use of the former supplying utility's transmission system—is likely to be present in some cases of municipal annexation. In the case of both new municipalizations and annexations, the bundled retail customers of a local utility become the bundled retail customers of a municipal utility (in one case a new municipal utility, in the other an existing municipal utility) *that will use the transmission system of the retail customers' former supplier in order to access other suppliers.*

As we explain above, in a "retail-turned-wholesale customer" situation, such as the creation of a municipal utility system, a newly-created entity becomes a wholesale power purchaser on behalf of the retail customers. It is the conduit by which retail customers, if they cannot obtain direct retail access, can reach power suppliers other than their historical local utility power supplier. Although the retail customers remain bundled retail customers, in that they become the bundled customers of the new entity, we call this a "retail-turned-wholesale customer" situation because the new entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission, access and new power supply. The same analogy applies to newly annexed customers; they become "new" wholesale customers in the sense that the wholesale entity obtains transmission and new power supply on their behalf.

Accordingly, we clarify that this Commission will be the primary forum for addressing the recovery of stranded costs if an existing municipal utility uses the transmission system of its annexed retail customers' former supplier to access new suppliers to serve the annexed load. As long as Commission-required transmission access (the former supplier's open-access tariff or transmission services ordered under FPA section 211) is the vehicle that enables an existing municipal utility to obtain power supplies to serve annexed loads, we believe that any costs

stranded as a result of this wholesale transmission access are properly viewed as economic costs that are jurisdiction to this Commission. In such a case, the bundled retail customers that are annexed by an existing municipal utility would, through the municipal utility, use the transmission system of their former supplier to obtain access to new supplies and thereby expose their former supplier to non-recovery of prudently incurred costs. As in the case of new municipal systems that use the transmission system of their retail customers' former supplier, such costs would not be stranded but for the action of this Commission in requiring a utility to make unbundled transmission services available.[690]

Just as we will not be the primary forum for stranded cost recovery for *all* new municipalizations, so also we will not be the primary forum for stranded costs recovery for *all* cases of municipal annexation. Instead, our holding is limited to those cases in which the existing municipal system uses Commission-mandated transmission access from the annexed customers' former supplying utility to obtain power from a new supplier. Costs that are exposed to nonrecovery when an existing municipal utility *does not* use the transmission system of the retail customers' former supplier to reach a new generation supplier (*e.g.*, through self-generation or use of another utility's

[690] SoCal Edison requests clarification that a transaction in which a retail customer disconnects from a utility's system and accesses another generation supplier by interconnecting with a public power entity, who in turn would interconnect with a neighboring jurisdictional utility, constitutes a municipalization, not an expansion of a service territory. Because we have decided to treat municipal annexations (or expansions) and new municipalizations similarly for purposes of stranded cost recovery under the Rule. SoCal Edison's request is moot to the extent, that it envisions a scenario in which the former supplier's transmission system is used to access a new generation supplier. However, as discussed below, the rule would not provide an opportunity to seek recovery of stranded costs if the municipal entity in the scenario described by SoCal Edison *dose not* use the former supplier's transmission system.

transmission system) do not meet the definition of "wholesale stranded costs" for which the rule provides an opportunity for recovery. Such costs are outside the scope of the rule because such costs would not be stranded as a direct result of Commission-required transmission access.

We reject as misplaced the argument that the Commission, by failing to address costs that arise if a municipal utility (whether a *new* municipal utility or an existing municipal utility that annexes additional retail customer territory) does not use the historical supplying utility's transmission system, has not met its statutory obligation to "set just and reasonable" rates. The Commission in this rulemaking has not determined any utility's just and reasonable rates. Further, Order No. 888 does not by its terms bar the recovery of costs that do not result from the use of Commission-required transmission access. Utilities may, as before, seek recovery of such non-open-access-related costs on a case-by-case basis in individual rate proceedings. The Commission will not prejudge those issues here.

As we indicated in Order No. 888, we also are concerned that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open-access transmission, to circumvent the ability of any regulatory commission—either this Commission or state commissions—to address recovery of stranded costs.[691] We reiterate that we reserve the right to address such situations on a case-by-case basis.

We share the concern expressed by Puget that a retail-turned-wholesale customer should not be allowed to avoid any stranded cost obligation that it may have under Order No. 888 simply by having its new supplier be the entity that requests and contracts

[691] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,819; *mimeo* at pp. 536-37.

for transmission service from the former supplying utility. We clarify that the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers under Order No. 888 applies if the transmission system of the former supplier is used to transmit the newly obtained power supplies to the departing retail customer, regardless of whether the customer or its new supplier is the actual entity that requests and contracts for the unbundled transmission service. We have revised the definition of "wholesale stranded cost" in section 35.26(b)(1)(ii) accordingly to include the situation in which the retail customer subsequently becomes, either directly or through another wholesale transmission purchaser, an unbundled wholesale transmission services customer of the former supplying utility.

We clarify in response to SoCal Edison's request that our decision to be the primary forum for recovery of stranded costs from retain-turned-wholesale customers is not intended to prevent or to interfere with the authority of a state to permit any recovery from departing retail customers, such as by imposing an exit fee prior to creating the wholesale entity. As we indicated in Order No. 888, if the state has permitted any such recovery from a departing retail-turned-wholesale customer, that amount will not in fact be stranded. Accordingly, we will deduct that amount from the costs for which the utility will be allowed to seek recovery from this Commission.[692]

We clarify in response to SoCal Edison's request that the Commission has the discretion to defer to a state stranded cost calculation methodology. However, because we recognize that state retail access plans may present questions that need to be addressed on a case-by-case basis, we will consider whether to exercise that discretion on a case-by-case basis.

---

[692] *FERC Statutes and Regulations. Regulations Preambles January 1991-June 1996* at p. 31,819; *mimeo* at p. 537.

7. Recovery of Stranded Costs Caused by Retail Wheeling

In Order No. 888, we concluded that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in order to reach a different generation supplier, and that utilities are entitled, from both a legal and a policy perspective, to an opportunity to recover all of their prudently incurred costs.[693] We explained that this Commission's authority to address retail stranded costs (i.e., stranded costs associated with retail wheeling customers) is based on our jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, and that the authority of state commissions to address retail stranded costs is based on their jurisdiction over local distribution facilities and the service of delivering electric energy to end-users. Because it is a state decision to permit or to require the retail wheeling that causes stranded costs to occur, we decided we generally will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority[694] does not have authority under state law to address stranded costs when the retail wheeling is required. In such a case, we will permit a utility to seek a customer-specific surcharge to be added to an unbundled transmission rate.

---

[693] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,824-26; *mimeo* at pp. 553-58.

[694] "State regulatory authority" has the same meaning as provided in section 3(21) of the FPA: "'State regulatory authority' has the same meaning as the term 'State commission', except that in the case of an electric utility with respect to which the Tennessee Valley Authority has ratemaking authority (as defined in section 3 of the Public Utility Regulatory Policies Act of 1978), such term means the Tennessee Valley Authority."

We noted that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We indicated that rates for services using facilities used in local distribution to make a retail sale are state-jurisdictional, and that states will be free to impose stranded costs caused by retail wheeling on facilities or services used in local distribution. We also said that states may use their jurisdiction over local distribution facilities or services to recover so-called stranded benefits.

We stated that we believe our approach to stranded costs associated with retail wheeling customers represents an appropriate balance between federal and state interests that ensures that the rates for transmission in interstate commerce by public utilities (except in a narrow circumstance) will not be burdened by retail costs.

We expressed concern about the cost-shifting potential in a holding company or other multi-state situation, where denial of retail stranded cost recovery by a state regulatory authority could, through operation of the reserve equalization formula in a Commission-jurisdictional intra-system agreement; inappropriately shift the disallowed costs to affiliated operating companies in other states. We said that we will deal with such situations if they arise pursuant to public utility filings under section 205 or complaints under section 206. Thus, the need to amend a jurisdictional agreement to prevent stranded costs associated with retail wheeling customers from being shifted to customers in other states will be addressed on a case-by-case basis. We encouraged the affected state commissions in such situations to seek a mutually agreeable approach to this potential problem. If such a consensus solution resulted in a filing to modify a jurisdictional agreement, we indicated that we would accord such a proposal deference, particularly if other interested parties cannot reach consensus that would prevent cost shifting,

we said that the Commission would ultimately have to resolve the appropriate treatment of such stranded costs.

Rehearing Requests Opposing Any Commission Involvement in Stranded Costs Associated With Retail Wheeling Customers

A number of entities dispute the Commission's statement that both it and the states have the legal authority to address stranded costs that result from retail wheeling. Central Illinois Light contends that the Commission's claim of dual jurisdiction is inconsistent with *FPC v. Southern California Edison Company*.[695] It says that the court in that case recognized that Congress meant to draw a bright line easily ascertained between state and federal jurisdiction, making unnecessary case-by-case analysis. Central Illinois Light asserts that the Commission has stepped over the bright line into the states' exclusive jurisdiction over retail rates.

IA Com seeks rehearing on the Commission's assertion of concurrent jurisdiction with state authorities over stranded costs associated with retail wheeling customers on the ground that it is based on the Commission's erroneous assertion of jurisdiction over unbundled retail transmission.

IL Com says that regardless of whether the Commission's claim of jurisdiction over retail transmission is upheld, the Commission's ruling that there is joint jurisdiction over retail stranded costs is in error. According to IL Com, the Commission has no authority over such stranded costs. IL Com also disputes the Commission's characterization of the derivation of state authority to address such stranded costs. It says that state commission authority does not derive only from states' jurisdiction over local distribution facilities and the service of

---

[695] 376 U.S. 205, 215-16 (1964).

commission authority to address retail stranded costs derives from the existence of state commission jurisdiction over the facilities and costs at the time of their incurrence.

A number of entities contend that Commission jurisdiction over transmission facilities used in interstate commerce does not give it jurisdiction over stranded investment in retail generating assets.[696] Several argue that the fact that a retail wheeling customer might need transmission access from its former supplier does not change the character of the costs that are stranded. They maintain that retail stranded costs are not costs of providing unbundled transmission service, but are costs associated with providing what was formerly bundled retail service, over which the Commission has no jurisdiction.[697]

Several entities argue that it is solely the action of the state that allows a given utility's retail customers to seek alternative sources of supply; therefore, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime.[698]

A number of entities submit that the provision of FPA section 201 that federal regulation is "to extend only to those matters which are not subject to regulation by the States" bars any

---

[696] *E.g.*, Central Illinois Light, IN Consumer Counselor, IN Consumers, Nucor, FL Com, WI Com, VA Com, AR Com, MO/KS Com, OH Com, APPA,. For example, FL Com asserts that costs for facilities that are currently under the jurisdiction of state authorities do not become the Commission's jurisdiction because retail wheeling is instituted; in most cases, the sates approved both the construction and the cost recover for these facilities under bundled rate structures. FL Com submits that the states are in a better position to judge the extend and value of assets that may become stranded as a result of retail wheeling.

[697] *E.G.*, APPA, AR Com, MO/KS Coms, OH Com.

[698] *E.g.*, NARUC, TAPS.

attempt by the Commission to displace or supplant an admittedly legitimate exercise of state authority over retail stranded costs.[699] NASUCA submits that all state commissions have the authority to establish just and reasonable rates for the retail electric utilities in their respective jurisdictions.[700] It maintains that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws; the Commission has no knowledge or expertise regarding the specific state legal frameworks in which these costs were included in rates. NY Com argues that the Commission does not have jurisdiction to determine the rate treatment of costs devoted to retail service and, thus, lacks authority to allow recovery if a state decides to do so.

VA Com argues that section 201(b)(1) of the FPA restricts the Commission's jurisdiction to wholesale sales. It says that a departing retail customer remains a retail customer, regardless of the supplier. VA Com concludes that no portion of the transaction is a wholesale sale, and that there are no wholesale costs associated with a retail wheeling transaction.[701]

---

[699] *E.g.*, NASUCA, NY Com, WY Com, NARUC. The Consumer's Utility Counsel Division of the Georgia Governor's Office of Consumer Affairs filed comments on June 24, 1996, in support of NARUC's request for rehearing on the jurisdictional issues pertaining to the recovery of retail stranded costs. While answers to request for rehearing generally are not permitted, 18 C.F.C. §385.213(a)(2) (1996), we will depart from our general rule because of the significant nature of this proceeding and will accept these comments.

[700] According to NASUCA, whether or not that authority includes a requirement that a utility receive 100 percent return on stranded costs (or something less) is a matter to be determined by the state courts and legislatures.

[701] *See also* AR Com (one retail transaction is replaced by another retail transaction; there is no wholesale transaction and no wholesale costs over which the Commission has jurisdiction).

A number of entities seek rehearing of the Commission's decision that it will entertain stranded cost claims when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required.[702] NARUC submits that Congress did not intend the Commission to become involved in adjudicating legal questions regarding the breadth of state law authority granted state commissions by their legislatures. NARUC expresses concern that the Commission would second-guess a state cost recovery determination and promote forum shopping. Once a balance has been struck at the state level concerning the terms of restructuring, NARUC submits that it is inconceivable that the Commission would have either the desire or authority to second-guess a state's legislative and regulatory processes.

Several entities object that the Commission effectively would authorize recovery of stranded costs associated with a retail wheeling customer if a state legislature withholds from the state regulatory agency the authority to approve stranded cost recovery.[703] They submit that just because a state has not given its regulatory commission the authority to impose stranded costs in the case of retail wheeling does not confer jurisdiction on the Commission to impose such charges. They contend that the state legislature should be the final arbiter of state policy. IL Com submits that if a state legislature chooses not to give its state commission the authority to act on stranded costs, "that can be taken as a clear indication that the state's legislature most certainly does not want FERC to address them."[704] Central

---

[702] *E.g.*, NARUC, Central Illinois Light, IN Com, American Forest & Paper, IN Consumer Counselor, IN Consumers, IL Com.

[703] *E.g.*, Central Illinois Light, IN Com, American Forest & Paper, IN Consumer Counselor, IN Consumers, IL Com, TX Com considers that it has the power to address stranded cost issues related to retail transmission service.

[704] IL Com at p. 38 (emphasis in original).

Illinois Light objects that the Commission has offered no reason why it will accept the decision of the regulatory agency, but not that of the legislature.

AMP-Ohio and Cleveland ask the Commission to clarify that its deference to the determinations of the states is to the authority of the states as exercised through state legislative bodies (and other political subdivisions with legislative authority) as well as to state regulatory bodies. They submit that if the state legislature, or a local government acting in accordance with its authority, enacts retail wheeling legislation that expressly limits the ability of its regulatory body to permit recovery of stranded costs, even barring all such recovery, the Commission should not become involved.

Several entities ask the Commission to clarify that Order No. 888 does not permit utilities to apply to the Commission for recovery of stranded costs associated with a retail wheeling customer when a state regulatory authority has "addressed" a request for the same stranded costs but has not allowed 100 percent recovery,[705] ELCON gives two hypothetical examples to which it asks the Commission to respond; one where a state regulatory authority possesses full stranded cost recovery authority but allows only 50 percent recovery; the other where the state legislature provides the state regulatory authority by statute with the power to permit recovery of up to 50 percent of identified stranded costs.

Commission Conclusion

We reaffirm our conclusion that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in interstate

---

[705] *E.g.*, ELCON, NASUCA, IL Com. NY Com.

commerce from public utilities in order to reach a different generation supplier, but that, because it is a state decision to permit or require the retail wheeling that causes retail stranded costs to occur, we will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required.

We will reject the requests for rehearing that oppose any Commission involvement in stranded costs associated with retail wheeling customers. We disagree with those entities that challenge our conclusion that both this Commission and the states have the legal authority to address stranded costs that result from retail wheeling (variously described by those entities as dual, concurrent, or joint jurisdiction). The Commission explained in detail in Order No. 888 the legal basis for concluding that this Commission and the state commissions each have jurisdiction over separate aspects of a retail wheeling transaction.[706] This Commission has jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities. State commissions have jurisdiction over local distribution facilities and the service of delivering electric energy to end-users. Based on our respective jurisdictions over separate aspects of the retail wheeling transaction, we believe either has the authority to provide the former supplying utility with an opportunity to recover costs stranded when the departing customer uses retail transmission in interstate commerce to reach a new supplier, but that here, unlike the retail-turned-wholesale scenario, the state commission should be the primary forum because these costs are stranded by

---

[706] *See FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,780-85; *mimeo* at pp. 427-42 and appendix G.

the action of the state. We would act only if the primary forum is not available. We have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity to seek recovery of prudently incurred costs.

Several entities argue that the Commission does not have jurisdiction over stranded investment in retail generating assets, that use of Commission-jurisdictional transmission does not change the character of the costs that are stranded, that stranded costs associated with retail wheeling customers are not costs of providing unbundled transmission service, but are costs associated with providing what was formerly bundled retail service, and that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws. While we agree that stranded costs associated with retail wheeling are costs that are retail in character in the sense that they are in retail bundled rates and become stranded as a result of retail wheeling required by the state commission, we do not believe this precludes the Commission from exercising jurisdiction in the limited circumstances of the Rule.

As an initial matter, we note that there are rarely separate retail and wholesale generating facilities. Retail customers and wholesale requirements customers get energy from the same facilities, each buying a "slice of the system." Typically all generating assets go into both the retail and the wholesale rate bases for determining retail and wholesale rates. Rates are determined by allocating the total generating costs among customer classes. The parties confuse the issue before us to the extent they suggest that state commissions, not this Commission have "jurisdiction" over certain "costs". Neither the state commissions nor this Commission has exclusive jurisdiction over "costs." Each regulatory authority has jurisdiction to determine "rates" for services subject to its jurisdiction and, in determining rates, may take into account all of the costs incurred by the

utility. Under historical cost-of-service ratemaking, each regulatory authority, in exercising its respective *ratemaking* jurisdiction, reviews the total costs incurred by a utility to provide service and makes its separate and independent determination of what costs may be recovered through rates within its jurisdiction.[707] Generating costs continually shift between retail and wholesale rates over time.[708]

More importantly, both the state commission and this Commission have a responsibility to oversee the financial health of the utilities we regulate. Each has jurisdiction to make judgment about recovery of the costs of the assets in the utility's

[707] If a utility is regulated by both this Commission and a state commission, each commission, in setting cost-of-service rates within its jurisdiction, will separately and independently determine the utility's *total* cost of providing service (also known as the utility's total revenue requirement). This will be based on the expenses incurred in providing service and a reasonable profit on the utility's assets that are used to provide the service. The commissions may differ as to what assets are appropriately included in total rate base, what other costs are appropriately included in the total cost of service, and what rate of return should be permitted. Once each regulatory authority has determined the appropriate total revenue requirement, it then will determine what portion of that total revenue requirement should be borne by the utility's wholesale customers and what share should be borne by retail customers (also-called cost allocation). Each commission may also reach different conclusions on this split as well. Thus, under historical cost-based ratemaking, regulatory authorities do not carve out so-called "wholesale costs" that only this Commission can take into account in determining rates subject to its jurisdiction or so-called "retail costs" that only a state commission can take into account in determining rates subject to state jurisdiction. Additionally, this Commission and state commissions have the discretion to determine whether costs are appropriately recovered through a transmission, generation, or distribution component of a rate (so-called functionalization of costs) within their respective jurisdictions.

[708] We reject arguments that stranded retail generation costs are not a cost of providing unbundled retail transmission. While such costs are not a cost of operating the physical transmission system, nevertheless, they are an economic cost incurred as a result of being required to provide retail transmission.

total rate base. Utilities are entitled to a regulatory forum that can adjudicate claims that they are or are not entitled to recovery of costs incurred regardless of the initial retail or wholesale "character" of those costs, and we believe we have the authority and obligation to fill a regulatory "gap" that could occur.[709]

In response to the argument that it is solely the action of the State that allows a retail customer to seek alternative sources of supply and, as a result, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime, we agree. Indeed, as we indicate in Order No. 888, we decided to leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling (with a limited exception) because it is a state decision to permit or require the retail wheeling in the first instance that causes retail stranded costs to occur. Our determination, as explained above, is to fill any regulatory gap that arises as a result of interstate wheeling. We believe that it is necessary for the Commission to act as a backstop in this limited instance to ensure that costs stranded as a result of retail wheeling do not go unrecovered because the state regulatory authority lacks the authority under state law to address such costs. At the same time, as we stated in Order No. 888, we believe that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We emphasize that this rule is not intended to preempt the exercise

[709] This is not a regulatory "gap" in the sense that the Commission would be asserting authority over matters not within its jurisdiction. However, the Commission would be filling a regulatory "gap" to the extent that the utility normally would have the opportunity to seek approval from its state regulatory commission to recover costs in retail rates from a departing retail customer or to reallocate those costs to other retail customers. In circumstances where the utility does not have this opportunity because the state regulatory authority has no authority to address the issue, we may appropriately fill this regulatory "gap" to permit recovery from the departing customer through the retail transmission rate.

of any existing state authority with respect to the assessment of a stranded cost or stranded benefits charge on a retail customer that obtains retail wheeling.

In response to arguments that the Commission's decision will result in second-guessing or interfering with a state's legislative processes and decisions, we believe these arguments are premature. As a general matter, we do not expect that our decision to be a backstop will interfere with legislative decisions that specifically address stranded cost matters and the scope of the state regulatory authority's authority in determining stranded costs. If states or parties to a retail stranded cost recovery case brought before this Commission believe that a Commission decision on the issue would interfere with state legislative decisions, they should raise their arguments, and support therefor, at that time.

We clarify that Order No. 888 does not permit utilities to seek recovery from the Commission of stranded costs associated with retail wheeling customers if a state regulatory authority with authority to address retail wheeling stranded costs has in fact addressed such costs, regardless of whether the state regulatory authority has allowed full recovery, partial recovery, or no recovery.

Rehearing Requests Supporting Broader Jurisdiction Over Stranded Costs Associated With Retail Wheeling Customers

A number of entities seek rehearing of the Commission's decision not to serve as a backstop for all stranded costs associated with retail wheeling customers. Some assert that the Commission has the legal authority to address independently stranded costs that arise from retail wheeling and that the Commission cannot lawfully abdicate or delegate such authority

to the states.[710] Coalition for Economic Competition submits that the Commission correctly concluded that it has jurisdiction over retail transmission rates, terms and conditions and the authority to address retail wheeling stranded costs. Thus, it argues that the Commission is without the power to make a "policy determination" that results in the Commission not exercising its legal authority over stranded costs associated with retail wheeling customers. It asserts that, just as the Commission recognizes that it "cannot simply turn over its jurisdiction" to the states to determine facilities subject to Commission jurisdiction,[711] the Commission cannot turn over its jurisdiction to establish stranded cost charges that it correctly determined it has the authority to establish. Coalition for Economic Competition argues that the Commission should adopt a stranded cost recovery policy similar to the policy the Commission has adopted with respect to the determination of state/federal jurisdiction, whereby the Commission would defer to state stranded cost determination so long as they are consistent with the Commission's policy.

Utilities For Improved Transition argues that the Commission's authority over public utility rates for the transmission of electric power, both wholesale and retail, is plenary and exclusive. As a result, it submits that the Commission may not avoid responsibility for costs stranded by transmission of retail power.[712] Illinois Power contends that

---

[710] *E.g.*, Utilities For Improved Transition, Coalition for Economic Competition.

[711] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,784; *mimeo* at p. 439.

[712] Utilities For Improved Transition argues that, based on *Consolidated Edison Company of New York, Inc.*, 15 FERC ¶ 61,174, at p. 61,405 (1981) and other cases, the Commission has jurisdiction over the entire delivery service (rendered on both the transmission and local distribution facilities)

Congress did not authorize the Commission to reject jurisdictional rate filings whenever the Commission regards the state commissions as a more convenient or appropriate forum.

EEI and the Coalition for Economic Competition contend that virtually all retail stranded costs can only occur through the vehicle of Commission-jurisdictional transmission in interstate commerce. They submit that the Commission, having recognized the clear nexus between FERC-jurisdictional transmission and stranded costs in the retail-turned-wholesale context, cannot fail to recognize the same clear nexus in the retail wheeling context.

Utilities For Improved Transition says that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states' doing so; the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service.

Coalition for Economic Competition and Utilities For Improved Transition contend that the Commission must consider stranded costs that arise from retail wheeling in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. Coalition for Economic Competition maintains that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (*e.g.*, wholesale wheeling and new municipalizations) but to exclude them from other jurisdictional wheeling rates (*e.g.*, retail wheeling, municipal annexation, and

---

as a transmission transaction. Utilities For Improved Transition submits that states do not have authority over rates on local distribution facilities used to complete a transmission transaction.

bypass).[713] Utilities For Improved Transition says that the just and reasonable standard requires the Commission to backstop the states to ensure that there is full stranded cost recovery. It objects that Order No. 888's disposition of jurisdiction creates a problem of cross-class discrimination (wholesale versus retail) and interclass discrimination (some retail versus the remainder of the retail).

Coalition for Economic Competition further argues that the Commission's failure to address all stranded costs associated with retail wheeling customers will result in an improper taking under the Constitution.[714] It also argues that the Commission is not permitted to disregard its findings in Order No. 888 which, according to Coalition for Economic Competition, "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail wheeling, municipal annexation, and bypass stranded costs) is required.[715]

Illinois Power argues that the FPA does not authorize the Commission to discriminate among utilities based on the state of their residence, and that the Commission must allow all utilities to seek interstate rate recovery of just and reasonable retail stranded costs. Illinois Power asserts that the rule will lead to the absurd, unduly discriminatory result that utilities located in states whose legislatures have failed to provide for stranded cost recovery will be better off than those located in states that

---

[713] EEI states that the Commission did not rebut EEI's argument that the Commission's failure to address all retail stranded costs was unduly discriminatory.

[714] In support of its argument, Coalition for Economic Competition cites *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 602 (1944); *Duquesne Light Company v. Barasch*, 488 U.S. 299, 307-08 (1989).

[715] Coalition for Economic Competition at p. 14.

provide for only limited stranded cost recovery. It supports use of the Commission's statutory authority to establish a uniform, natural method for retail stranded cost recovery.

Coalition for Economic Competition also contends that the Commission's decision to let the states deal with retail stranded costs is arbitrary and capricious because the Commission failed to consider the arguments that stranded cost opponents will make before state commissions, such as that a state lacks jurisdiction to impose stranded cost charges or that the state imposition of such charges may be preempted or found to be an undue burden on interstate commerce. It further argues that the Commission's reliance on state jurisdiction over the service of delivering electric energy to the end-user does not reflect reasoned decisionmaking. It submits that the Commission has failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, in which case the state commission may have no jurisdiction over either the sale or the transmission of the energy and, accordingly, no authority to consider stranded costs.

A number of entities ask the Commission to act on requests for retail stranded cost recovery when the state commission lacks authority or has authority to order recovery, but has declined to do so or has only allowed partial recovery.[716]

Lastly, TX Com notes that section 35.26(d) (dealing with recovery of retail stranded costs) refers only to public utilities. It suggests that the omission of a reference to transmitting utilities appears to be inadvertent and should be corrected.

---

[716] *E.g.*, Centerior, Southern, SoCal Edison.

Commission Conclusion

The Commission will reject the requests for rehearing of our decision not to assume a backstop role for all stranded costs associated with retail wheeling customers. We explained in Order No. 888 that commenters that describe our action as an unlawful abdication or delegation of authority misconstrue the nature of our decision to leave stranded costs associated with retail wheeling customers (with a limited exception) to state regulatory authorities.[717] We have not "abdicated" or "delegated" to state regulatory authorities our jurisdiction over the rates, terms, and conditions of retail transmission in interstate commerce; if retail transmission in interstate commerce by a public utility occurs, public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.[718] Instead, we have made a policy determination that the recovery of stranded costs associated with retail wheeling customers—an

---

[717] We also explained that the case law they cite (which they refer to again in their rehearing requests) to support the proposition that an agency is not authorized to abdicate its statutory responsibility or to delegate to parties and intervenors regulatory responsibilities is factually distinguishable and inapposite. *See FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,825 and note 765; *mimeo* at pp. 554-55 and note 765.

[718] The entities who argue that the Commissions has abdicated or delegated its jurisdiction to the states misconstrue the Commission's jurisdiction to determine rates for unbundled transmission in interstate commerce as somehow including exclusive "jurisdiction" over "costs". However, as discussed above, neither this Commission nor the state commissions has exclusive "jurisdiction" over "costs". Rather, each has jurisdiction to determine "rates" for services subject to its jurisdiction. It is in the course of determining "rates" for unbundled transmission in interstate commerce that this Commission can take into account various costs incurred by a utility to provide jurisdictional service. A state commission can take those same costs into account in making its separate and independent determinations of what costs may be recovered through rates within its jurisdiction. See note 707, *supra*, and accompanying text.

issue over which either this Commission or state commissions could exercise authority by virtue of their jurisdiction over retail transmission in interstate commerce and over local distribution facilities and services, respectively—is primarily a matter of local or state concern for which the primary forum should be the state commissions. However, if the state regulatory authority does not have authority under state law to be the forum to address stranded costs when the retail wheeling is required, then we will entertain requests to recover such costs. As we explain above in response to the rehearing petitioners that oppose any Commission involvement in stranded costs associated with retail wheeling customers, we have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity to seek recovery of prudently incurred costs.[719]

We disagree with Coalition for Economic Competition's argument that our findings in Order No. 888 "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail wheeling and bypass stranded costs) is required, much less that the Commission has ignored the findings in Order No. 888. To the contrary, as we explain in section IV.J.1. it is not the purpose of this rule to allow utilities an opportunity to seek to recover "all" uneconomic costs that might be stranded when a customer leaves its utility supplier. We have fully explained our reasons for adopting an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of stranded cost recovery from retail customers, recognizes state commission

[719] Based on these same considerations, we reject Coalition for Economic Competition's request that the Commission assume a backstop role for all stranded costs associated with retail wheeling customers but defer to state stranded cost determinations so long as they are consistent with the Commission's policy.

jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures.

We disagree with those entities that contend that the Commission must consider retail stranded costs in order to satisfy our statutory obligation under the FPA to set just and reasonable rates. In determining just and reasonable rates for jurisdictional transmission service, which currently are determined on a cost basis, the Commission satisfies its statutory obligation under the FPA by allowing utilities an opportunity to recover their prudently incurred costs plus a reasonable rate of return. As we have explained above, this may include the costs of use of the physical transmission system, as well as economic costs incurred by the utility when it provides transmission service (e.g., stranded costs). However, in situations in which a state regulatory authority has the authority to address recovery of retail stranded costs, there is no regulatory "gap," and there is no obligation for this Commission to provide a second opportunity for recovery.[720]

We reject arguments that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (wholesale wheeling and new municipalizations) but to exclude them from other jurisdictional wheeling rates (retail wheeling in interstate commerce and use of another utility's transmission tariff), and that this policy somehow makes rates discriminatory. Recovery of this type of cost through a transmission rate is obviously not the norm, but is necessitated by the need to deal with the transition costs associated with this Rule. As discussed in detail in the Rule, the

[720] If the state regulatory authority is the forum before which to seek recovery, the utility may make whatever arguments it wishes regarding the justness and reasonableness of its rates, as well as any unconstitutional taking arguments it may have, before the state forum. Further, it can pursue appeals of unfavorable decisions through the state court system.

Commission has carefully balanced the interests of utilities as well as customers in concluding that the opportunity for stranded cost recovery through transmission rates should be permitted in only two general circumstances: (1) in the case of wholesale stranded costs, where there is a direct nexus to Commission-required transmission access; and (2) in the case of retail stranded costs, where there otherwise would be a regulatory gap because a state regulatory authority lacks authority under state law to address stranded costs at the time that retail wheeling is required. We see nothing in the FPA that precludes us from exercising this flexibility and, indeed, the parties have not pointed to anything that, in our opinion, precludes us from exercising this discretion.

We reject the argument that virtually all stranded costs associated with retail wheeling customers can occur only through the vehicle of Commission-jurisdictional transmission in interstate commerce, and therefore, that the same nexus between FERC-jurisdictional transmission and stranded costs that exists in the retail-turned-wholesale context is present in the retail wheeling context. We also disagree that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states doing so, and that the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service. The opportunity for stranded cost recovery set forth in this rule is based on the causal link between stranded costs and the availability and use of the Commission-required transmission tariff. It is true that in both the retail-turned-wholesale context and the retail wheeling context there is a limited nexus between stranded costs and Commission-jurisdictional access since, in both situations, the Commission has jurisdiction over the rates, terms and conditions of the transmission service and, therefore, the authority to permit stranded cost recovery through the transmission rates. However, the *causal nexus* to FERC-jurisdictional transmission and stranded costs in the two contexts

(retail vs. retail-turned-wholesale) is different. In the retail wheeling context, there is *no causal nexus* between stranded costs and transmission that has been *ordered by this Commission*. In the retail-turned-wholesale context, in contrast, the opportunity for a utility to seek recovery of stranded costs is grounded on the existence of a *direct causal nexus* between stranded costs and transmission that has been *ordered by this Commission*.

We will reject the rehearing petitions that ask the Commission to act on request for stranded cost recovery associated with retail wheeling customers not only when the state commission lacks authority, but also when the state commission has authority but either has declined to use it or has only allowed partial recovery. As explained above, our decision to entertain requests to recover stranded costs caused by retail wheeling in a limited circumstance (when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on our determination to fill any regulatory gap that arises in association with interstate transmission.

We will reject TX Com's request that the Commission clarify that section 35.26(d) (dealing with recovery of retail stranded costs), which refers only to public utilities, should also refer to transmitting utilities. The Commission's decision to act as a limited backstop in the case of stranded costs associated with retail wheeling customers is based on our jurisdiction under sections 205 and 206 of the FPA over the rates, terms, and conditions of retail transmission in interstate commerce. As a result, our ability to allow the recovery of such costs through a

surcharge on a section 205 unbundled transmission rate is necessarily limited to public utilities.[721]

Rehearing Requests Opposing Commission Treatment of Stranded Costs Associated with Retail Wheeling Customers in Holding Company Intra-system Agreement Cases

A number of entities oppose the Commission's proposal to address on a case-by-case basis whether jurisdictional intra-system agreements may need to be amended in order to prevent inappropriate cost-shifting that could occur if one state disallows stranded cost recovery associated with retail wheeling customers. IN Com objects that the problem is not the actions of one state or another, but rather the terms of the intra-system agreement.

AR Com objects that Order No. 888 is factually in error because a state's treatment of retail stranded costs under the Entergy System Agreement cannot shift costs to other jurisdictions.[722] It submits that whenever retail load changes, whether due to retail wheeling or any other factor, responsibility ratios under Entergy's reserve equalization schedule, MSS-1, will change and costs will shift irrespective of the regulator's treatment of retail stranded costs. AR Com says that MSS-1 reveals no changes in calculations due to retail treatment of stranded costs or any other retail ratemaking only "excess" capacity costs of intermediate gas and oil-fired plant are "shifted"

---

[721] We note that the definition of "retail stranded cost" in section 35.26(b)(5) mistakenly refers to " a public utility *or* transmitting utility" (emphasis added). We will revise the definition to remove the reference to "transmitting utility."

[722] *See also* MO/KS Coms (the cost-shifting problem does not arise because of a particular state treatment of stranded costs, it arises because Energy insists on recovering 100 percent of its costs even when some portion of the costs are not economical).

under the Entergy System Agreement. Although the Commission has the authority to amend intra-system agreements when wholesale cost allocations have become unjust and unreasonable. AR Com submits that the Commission does not have jurisdiction to reach to the state level and dictate what retail ratepayers should pay to shareholders. AR Com maintains that a FERC-jurisdictional intra-system agreement extends only to sales for resale (transactions among subsidiaries), and that if a holding company believes that an intra-system agreement is unduly discriminatory as a result of a state's disallowance of costs, the holding company can propose to amend it.[723]

AR Com argues that retail stranded costs fall to state jurisdiction regardless of whether the utility is a member of an interstate holding company, AR Com says that because the costs at issue are in retail rate base, any Commission influence over their recovery could occur only through preemption, but preemption of a state disallowance from retail rate base is possible only if there is a "trapped cost." AR Com submits that a disallowance of retail rate base cost cannot result in a trapped cost because there is no inconsistency between two agencies acting within their jurisdiction; the Commission has no jurisdiction to act. AR Com maintains that, unlike the Grand Gulf situation, the Commission has not mandated any Entergy generation costs into retail rate base. It further says that different state decisions regarding recovery of retail costs are not inconsistent decisions; they represent each state applying its law to its facts. According to AR Com, decisions by states leading to

---

[723] AR Com also objects to the Commission's description of the issue as involving not only holding companies, but also other multi-state situations. AR Com says that "[t]he mere fact that a company's territory crosses state lines does not automatically mean that all assets serve all customers, or that all customers are required to bear the economic risk associated with all assets, or that assets that at one time were solely state-jurisdictional can somehow, by virtue of a company's decision to expand across state lines, before FERC-jurisdictional" AR Com at p. 11.

less than full recovery could be deemed inconsistent decisions only if there were a federal guarantee of full cost recovery of retail costs, which there is not.

AR Com and MO/KS Coms assert that the Commission's proposal for holding company situations cannot apply to future holding companies, where there is no history of joint planning justifying cost equalization, nor can it apply to future investments. They contend that this would require an assumption that the utility subsidiaries of a registered holding company have planned, and should plan, together rather than separately (i.e., that interaffiliate transactions are always more efficient than nonaffiliate transactions), and that such assumption would be sound only if having the transaction occur between affiliates is inherently more efficient than having the transaction occur between an affiliate and a nonaffiliate.

Commission Conclusion

The comments raised for the most part are either premature or reflect a misunderstanding of the Commission's decision. Contrary to AR Com's argument, the Commission in Order No. 888 in no way asserted jurisdiction over state determinations of stranded costs associated with retail wheeling customers. We agree with AR Com that our jurisdiction extends only to sales for resale (and transmission in interstate commerce) and that a holding company can seek to amend an intra-system agreement if it believes the agreement is unduly discriminatory as a result of a state's disallowance of costs. However, a holding company also may seek to amend an agreement *before* any potential disallowances can occur, to keep cost-shifting from occurring. The fact is that intra-system agreements which involve wholesale sales among affiliate companies in different states could, through operation of their reserve equalization formulas, result in customers in one or more states having to indirectly bear stranded costs that are disallowed in another state, and the

Commission has a responsibility to prevent inappropriate cost-shifting. Such determinations can be made only on a case-by-case basis. Again, as we stated in Order No. 888, we encourage affected state commissions to propose mutually agreeable solutions to this potential problem.

8. Evidentiary Demonstration Necessary—Reasonable Expectation Stranded

In Order No. 888, the Commission concluded that a utility seeking to recover stranded costs must demonstrate that it had a reasonable expectation of continuing to serve a customer. We stated that whether a utility had a reasonable expectation of continuing to serve a customer, and for how long, will be determined on a case-by-case basis, and will depend on all of the facts and circumstances. We also determined that the existence of a notice provision in a contract would create a rebuttable presumption that the utility had no reasonable expectation of serving the customer beyond the specified period. We said that whether or not a contract contains an "evergreen" or other automatic renewal provision will be a factor to be considered in determining whether the presumption of no reasonable expectation is rebutted in a particular case.[724]

We also said that we would apply the reasonable expectation standard to retail-turned-wholesale customers. We explained that, before the Commission will permit a utility to recover stranded costs, the utility must demonstrate that it incurred such costs based on a reasonable expectation that the retail-turned-wholesale customer would continue to receive bundled retail service. Whether the state law awards exclusive service territories and imposes a mandatory obligation to serve would be

---

[724] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996*, at p. 31,831; *mimeo* at pp. 570-72.

among the factors to be considered in determining whether the reasonable expectation test is met in a particular case.[725]

We noted that Order No. 888 does not address who will bear the stranded costs caused by a departing generation customer if the Commission finds that the utility had no reasonable expectation of continuing to serve that customer. We indicated that we anticipate that, in such a case, a public utility will seek in subsequent requirements rate cases to have the costs reallocated among the remaining customers on its system. However, we stated that we were not prejudging that issue in the Rule.[726]

Rehearing Requests Opposing or Seeking Modification of the Reasonable Expectation Standard

APPA challenges the reasonable expectation standard as being too vague. It submits that the Commission has provided no guidance concerning application of the reasonable expectation standard, other than the state that it would decide the issue on a case-by-case basis. APPA objects that public utilities can exploit the uncertainty created by this standard, which will lead to costly and time-consuming litigation. IL Com supports replacing the reasonable expectation standard with a statutory, regulatory, contractual standard.

Several entities contend that there is no basis to conclude that the reasonable expectation test could ever be met. VT DPS and Valero submit that, since 1973, utilities have known that a refusal to wheel power could subject them to antitrust liability.

---

[725] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at p. 572. We indicated that the same procedures would apply to retail customers that obtain retail wheeling.

[726] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at pp. 572-73.

They say that Order No. 888 ignores the breadth of NRC licensing conditions. LEPA similarly argues that the reasonable expectation standard could not be met where NRC license conditions required an explicit wheeling commitment and prohibited the utility from including in the wheeling cost any amount attributable to the loss of customers due to the wheeling. It objects that delaying a decision on stranded cost recovery in such cases holds the threat of possible stranded cost charges over the heads of bulk power purchasers and thereby chills their ability to seek competitive sellers.

TAPS asserts that there should be an irrefutable presumption that no stranded costs are due from customers with preexisting transmission rights, including customers who were the beneficiaries of NRC license conditions.[727] TAPS submits that there can be no legitimate "reasonable expectation" that such customers would continue to purchase power if the price was higher than the market price.

Occidential Chemical asks the Commission to clarify that a utility could have had no reasonable expectation of recovering stranded costs from customers who, prior to the issuance of the NOPR, had the opportunity to switch to an alternative electric supplier or had the option of self-generating, obtaining on-site third-party generation, or municipalizing. Occidental Chemical further argues that it defies commercial expectations to allow a utility to argue that if a contract is silent on the issue of renewal, the obligation to purchase does not expire with the termination of the contract. It submits that the Commission has not shown that it has the authority to force customers to extend purchase agreements against their will in violation of accepted commercial practice.

---

[727] AMP-Ohio submits that where transmission access and competition have existed to varying extent for decades, there should be an irrebuttable presumption of no reasonable expectation of continued service.

A number of entities submit that the Commission erred in failing to treat a notice of termination provision as conclusive evidence that the utility had no reasonable expectation of continued service.[728] Several object that the Commission has failed to explain why the present of a notice provision does not conclusively demonstrate the lack of a reasonable expectation and *ipso facto* terminate the obligation of the customer to purchase the product.[729] APPA objects that the Commission provided no evidence that it considered comments supporting making the presumption conclusive and that it found legally sufficient reasons to reject them.

PA Munis objects that the rebuttable presumption represents an unjustified departure from the Commission's traditional policy of enforcing the express terms of notice provisions without any inquiry into the reasonable expectations of the party, provided that the agreements were negotiated in good faith and approved by the Commission.[730] PA Munis contends that wholesale requirements customers negotiated notice provisions with the knowledge that the Commission would enforce the notice provisions according to their terms, including the specific length of the term.[731] PA Munis argues that it is arbitrary and capricious to provide utilities an opportunity to seek to amend these contracts.

---

[728] *E.g.*, APPA, American Forest & Paper, Central Montana EC, NRECA, TDU Systems, Oglethorpe, IMPA, VT DPS, Valero, PA Munis.

[729] *E.g.*, APPA, NRECA, TDU Systems. *See also* VT DPS and Valero (by signing a contract with a termination date, the utility assumed the risk that the customer will elect to leave when the contract expires).

[730] In support of its argument, PA Munis cites *Boston Edison Company*, 56 FPC 3414 (1976). *See also* American Forest & Paper.

[731] *Citing Kentucky Utilities Company*, 23 FERC ¶ 61, 317 (1983); *Philadelphia Electric Company and Susquehanna Electric Company*, 65 FERC ¶ 61,303 (1993).

Several entities submit that the rebuttable presumption invites litigation and promotes uncertainty for customers.[732] APPA objects that the Commission has failed to establish the showing that it would require to overcome the presumption.

Referring to the Commission's discussion of evergreen provisions, Central Montana EC argues that it is wrong to infer from the existence of an automatic renewal provision that the parties intended that the contract might run longer than its initial term. Central Montana EC asserts that the presence of an evergreen provision infers simply that the parties agreed upon a mechanism to avoid the renegotiation of a power supply contract if, at the conclusion of its initial term, the parties were satisfied with the contract. It maintains that the parties' obligations are defined by the term and termination provision of wholesale power contracts, and that the presence of a mechanism to avoid contract renegotiation does not alter those termination rights.

Commission Conclusion

We will reject the requests for rehearing of our decision to adopt a reasonable expectation standard to be applied on a case-by-case basis and to treat a notice provision in a contract as a rebuttable, not a conclusive, presumption of no reasonable expectation. Contrary to the claims of some entities, the Commission has explained the basis for its finding that utilities may have had an implicit obligation to serve their wholesale requirements customers and, therefore, that a utility should be given an opportunity to demonstrate that it incurred costs to provide service to a customer and that it had a reasonable expectation that it would continue to serve the customer beyond the contract termination date. The same factors that some petitioner contend establish the absence of a reasonable

---

[732] *E.g.*, NRECA, IMPA, PA Munis.

expectation of continued service may be offered as evidence to be considered in determining whether the reasonable expectation test is met in a particular case.

We believe that our decision to treat a notice of termination provision in a contract as creating a rebuttable presumption that the utility had no reasonable expectation of serving the customer beyond the period provided for in the notice provision is a reasonable one. It places evidentiary significance on the fact that a contract contains a notice of termination provision. Moreover, while it gives the utility an opportunity, based on the facts and circumstances of a particular case, to rebut the presumption of no reasonable expectation, it firmly places the burden of establishing reasonable expectation on the utility. Although some entities support treating notice provisions as a conclusive presumption of no reasonable expectation, as discussed below, we decline to adopt such an inflexible approach. Nevertheless, as we indicated in Order No. 888, when a utility is seeking a contract amendment to permit stranded cost recovery based on expectations beyond the stated term of the contract, we believe that the utility has a heavy burden in demonstrating that the contract ought to be modified.[733]

Contrary to the position of PA Munis, the rebuttable presumption is fully consistent with the Commission's past treatment of notice provisions. For example, the *Kentucky Utilities Company* case cited by PA Munis supports the proposition that, until a customer *exercises* a notice of termination provision, the utility is under an implicit obligation to continue to serve and plan for the future needs of the

[733] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,665, 31,813-14; *mimeo* at p. 87,522.

customer.[734] Thus, the presence of a notice of termination provision in a contract (particularly one not yet exercised by the customer), in and of itself, may not necessarily support the conclusion that the utility could never prove that it reasonably expected to continue serving the customer beyond the notice period.[735]

In response to APPA's objection that the Commission has failed to establish the showing that it would require to overcome the presumption, we note that the Commission cannot establish such a showing upfront because whether there is sufficient evidence to rebut the presumption of no reasonable expectation will depend on the facts of each case.

We appreciate the concerns expressed by some entities that the rebuttable presumption may increase the customer's uncertainty by inviting litigation. We have carefully weighed the pros and cons of treating a notice provision as a rebuttable presumption of no reasonable expectation versus the pros and cons of treating it as a conclusive presumption of no reasonable expection. It is true, as some entities assert, that the rebuttable presumption approach presents the potential for litigation between the parties as to whether, in a particular case, the utility can rebut the presumption. The alternative would be to treat all contracts with notice of termination provisions as conclusive evidence that the utility could have had no reasonable

[734] *See Kentucky Utilities Company*, 23 FERC at pp. 61,679-80 ("Once it receives an effective notice of cancellation, Kentucky can stop planning for the future needs of that customer ... To be effective a notice of cancellation must contain a specification of the source of supply, the date on which the source of supply will be available, and an affidavit from the supplier that it will supply the customer on the date the contract ends").

[735] *See Potomac Electric Power Company*, 43 FERC ¶ 61,189 (1988) (suspending a notice of termination for five months due to questions about the impact of the proposed cancellation on service reliability).

expectation it would continue to serve the customer beyond the specified notice period. While the latter approach presumably would reduce the number of cases in which the issue of a utility's reasonable expectation would have to be litigated, it would do so only by prohibiting a utility from ever demonstrating that, notwithstanding the existence of a notice provision, based on the facts of a particular case, the utility reasonably expected to continue serving the customer. While we do not prejudge the likelihood of a utility being able to rebut the presumption in a particular case, we believe that it would not be in the pubic interest for the Commission to absolutely preclude a utility from being able to make such a showing. On this basis, we conclude that treating a notice provision as a rebuttable, rather than a conclusive, presumption that the utility did not have a reasonable expectation of continuing service to the customer is, on balance, the fairer and more equitable approach.

Central Montana EC asserts that it is wrong to infer from the existence of an automatic renewal provision that the parties intended that the contract might run longer than its initial term. However, our statement in Order No. 888 that the existence of an automatic renewal provision will be a factor to be considered in determining whether the presumption of no reasonable expectation is rebutted in a particular case makes no such inference. Whether the utility can rebut the presumption will depend on the facts of each case.

Rehearing Requests Supporting Modification of Evidentiary Standard for Retail Customers

Several entities ask the Commission to consider adopting a rebuttable presumption that utilities had a reasonable expectation of continuing to serve any retail load for which they had a public utility obligation to serve. They submit that the burden should be on the former bundled retail customer to show that the utility's service obligation was not binding and that the utility's

expectation of continuing service was unfounded.[736] Florida Power Corp and Utilities For Improved Transition suggest that the only exception to such a rebuttable presumption should be for retail customers that gave notice of termination before the effective date of the Rule. EEI expresses concern that the issue may be wrongly decided on the existence (or lack) of any exclusive franchise. It states that while many states do award franchises delineating exclusive service territories, some do not, even though long-established service arrangements are in place. Puget submits that because there is a duty to serve all retail customers. Order No. 888 should provide for stranded cost recovery from all departing retail customers without application of a reasonable expectation test.

NY Com, on the other hand, opposes application of the reasonable expectation standard to stranded costs associated with retail-turned-wholesale customers. It argues that the reasonable expectation test would ignore prudence, customer impact, financial viability and a series of criteria traditionally analyzed by state regulatory agencies in determining rate treatment of costs incurred with the intention of providing service.

Commission Conclusion

We will deny the requests for rehearing of the Commission's decision to apply the reasonable expectation standard to retail-turned-wholesale and retail wheeling customers on a case-by-case basis without adopting a rebuttable presumption that utilities had a reasonable expectation of continuing to serve any retail load for which they had a public utility obligation to serve. When a utility seeks to recover stranded costs from former

---

[736] *E.g.*, EET, Oklahoma G&E, Southern, Florida Power Corp., Utilities For Improved Transition.

bundled retail customers, we think it is appropriate that the utility bear the burden of proving reasonable expectation (instead of requiring the customer to bear the burden of disproving the utility's reasonable expectation). Placing the burden on the utility is consistent with the requirement of sections 205 and 206 of the FPA that a public utility demonstrate the justness and reasonableness of its proposed rates. The same factors that are offered as support for the establishment of a rebuttable presumption of a reasonable expectation (such as the utility's obligation to serve all retail customers) may be offered by the utility as evidence to be considered in determining whether the reasonable expectation test is met in a particular case.

We also will deny NY Com's request that the Commission not apply the reasonable expectation standard to retail-turned-wholesale customers. We believe it is appropriate to require the same evidentiary demonstration for recovery of stranded costs from a retail-turned-wholesale customer as that required in the case of a wholesale requirements customer. Moreover, as discussed in section IV.J.7 above, the reasonable expectation standard contemplates evidence as to what a utility might reasonably expect to recover under state law, and we will give great weight to a state's view of what might be recoverable.

9. Calculation of Recoverable Stranded Costs

In Order No. 888, the Commission considered various proposals regarding how stranded costs should be calculated and who should pay. With respect to the calculation of stranded costs, the Commission rejected as overly complicated and costly an asset-by-asset approach to determine the amount of stranded costs assigned to a departing customer. Instead, the Commission determined that the revenues lost approach was the fairest and most efficient way to make this determination during the transition to a competitive wholesale bulk power market. The Commission adopted the following revenues lost formula for

calculating the stranded cost for each departing customer. SCO = (RSE — CMVE) x L. The Commission provided a precise definition for each component of the formula,[737] and made the application of the formula, and collection of the resulting stranded costs, subject to a number of conditions.[738]

RSE Issues

Numerous petitioners oppose the use of present revenues in the stranded cost forumla.[739] TDU Systems argues that the revenues lost approach is arbitrary and capricious because its effect exceeds its purpose. Specifically, TDU Systems contends that the revenues lost approach can permit over-recovery because it provides recovery of any difference between pre-Order No. 888 cost-plus rates and post-Order No. 888 competitive rates, regardless of the cause of the difference. TDU Systems cites enhanced utilization and technological improvements as two examples of pre- and post-Order No. 888 rate differences that are not competition related, but for which recovery would be provided. TDU Systems states that instead of using present revenues, RSE should be calculated based on the most current, reliable estimate of future revenues.

---

[737] Briefly, SCO refers to the departing customer's stranded cost obligation, which is determined by taking the average annual revenues that the customer would have paid had it remained a customer of the utility (RSE), and subtracting from it the competitive market value of the power (on an average annual basis) no longer taken by the departing customer (CMVE). The difference represents the average annual stranded cost, which must be multiplied by "L" (L represents the period over which the utility reasonably could have expected to serve the departing customer beyond the contract termination, but for the open access required under Order No. 888 to produce the departing customer's total SCO.

[738] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,839-40; *mimeo* at pp. 595-99.

[739] *E.g.*, TDU Systems, APPA, Central Vermont, ELCON.

Multiple Intervenors argues that the revenues lost method assumes that a utility's costs of operating its plants are *per se* reasonable, yet the New York utilities' current rates include levels of O&M, especially wages and benefits, expenses that may reflect inefficiencies and thus are not stranded costs for which a utility's shareholders should be compensated. Similarly, other petitioners oppose as backward-looking the use of present revenues for what should be a forward-looking remedy, consistent with the other elements in the formula.[740] TDU Systems argues that the use of past revenues is inappropriate in a falling cost environment, and notes that new capacity costs are less than the existing capacity costs embedded in a utility's rate base.

NYSEG states that the Commission should permit a utility to reconcile initial stranded cost charges to actual stranded costs on a periodic basis to account for changes in sales, energy purchases from NUGs, and changes in market price. NYSEG supports development of stranded cost charges based on three-year estimates. Under this approach, a customer would pay locked-in charges for a series of three-year periods. At the end of each period, the stranded cost estimate would be revised for the next three-year period. This process would continue until all stranded costs are recovered.[741] Other petitioners support the use of a projected revenue stream or a true-up mecha-

* * * * *

---

[740] *E. g.*, TDU Systems, NRECA, Central Montana EC, SoCal Edison.

[741] *See also* Coalition for Economic Competition at p. 47.

(2) Supreme Court, U.S.
FILED
00 568 OCT 12 2000
OFFICE OF THE CLERK

No.

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK and THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioners,

-v-

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

PETITION FOR A WRIT OF CERTIORARI
Volume II

LAWRENCE G. MALONE*
General Counsel
JONATHAN D. FEINBERG
DIANE T. DEAN
Assistant Counsel
NYS-Dept. of Public Service
Public Service Commission
3 Empire State Plaza
Albany, NY 12223-1350
(518) 474-2510

**Counsel of Record*

October 11, 2000

(Additional Counsel on Inside Cover)

260 pp

CHARLES D. GRAY
National Association of
Regulatory Utility Commissioners
1100 Pennsylvania Avenue, N.W.
Suite 603, P.O. Box 684
Washington, D.C. 20044-0684
(202) 898-2208

CATHERINE BEDELL
General Counsel
RICHARD BELLAK
Associate General Counsel
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Fl 32399-0850
(850) 413-6092

ALAN G. LANCE
Attorney General
DONALD L. HOWELL, II
Deputy Attorney General
Idaho Public Utilities Commission
472 West Washington Street
P.O. Box 83720
Boise, ID 83720-0074
(208) 334-0312

JOHN J. FARMER, JR.
Attorney General
State of New Jersey
By: HELENE S. WALLENSTEIN
Sr. Deputy Attorney General
Attorney for New Jersey Board
of Public Utilities
124 Halsey Street 5th Floor
P.O. Box 45029
Newark, NJ 07101
(973) 648-4846

JOANNE SANFORD
North Carolina Utilities
Commission
ROBERT P. GRUHER
Public Staff, North Carolina
Utilities Commission
GISELE L.RANKIN
Staff Attorney
P.O. BOX 29520
RALEIGH, NC 27626-0520
(919) 733-2435

WILLIAM H. CHAMBLISS
General Counsel
C. MEADE BROWDER, JR.
Attorney Virginia State
Corporation Commission
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218
(804) 371-9671

CHRISTINE O. GREGOIRE
Attorney General
WILLIAM BERGGREN COLLINS
Senior Assistant Attorney General
ROBERT D. CEDARBAUM
Senior Counsel for the Washington
Utilities and Transportation Commission
P.O. Box 40128
Olympia,WA 98504-0128
(360) 664-1188

HARVEY L. REITER
for the Vermont Department of
Public Serice
MORRISON & HECKER
1150 18th Street, N.W., Suite 800
Washington, D.C. 20036
(202) 785-9100

HARRY IVEY
for the Wyoming Public Service
Commission
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002
(307) 777-7824

THE REPORTER COMPANY, *Printers and Publishers, Inc.*
181 Delaware Street, Walton, NY 13856—800-252-7181
(2817 – 2000)

Printed on Recycled Paper

APPENDIX F

81 FERC Section 61,248 (Order 888-B)

[¶ 61,248]

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities, Docket No. RM95-8-003

Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Docket No. RM94-7-004

Order No. 888-B; 62 Fed. Reg. 64688

(Issued November 25, 1997)

Before Commissioners; James J. Hoecker, Chairman, Vicky A. Bailey, and William L. Masey

Agency: Federal Energy Regulatory commission.

Action: Order No. 888-B (Order on Rehearing).

Summary: The Federal Energy Regulatory Commission (Commission) affirms, with certain clarifications, the fundamental calls made in Order No. 888-A

Effective Date: The tariff change ordered if the order on rehearing (see footnote 1) will become effective on February 9, 1998. The current requirements of Order Nos. 888 and 888-A will remain in effect until this order becomes effective.

For Further Information Contact: David D. Withnell (Legal Information—Docket No. RM95-8-003). Office of the General Counsel, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-2063

Deborah B. Leahy (Legal Information—Docket No. RM94-7-004), Office of the General Counsel, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-2039

Daniel T. Hedberg (Technical Information—Docket No. RM95-8-003), Office of Electric Power Regulation, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-0243

Joseph M. Power (Technical Information—Docket No. RM94-7-004), Office of Electric Power Regulation, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-0243

Supplementary Information: In addition to publishing the full text of this document in the *Federal Register,* the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in Room 2A, 888 First Street, NE., Washington, DC 20426. The complete text on diskette in WordPerfect format may be purchased from the Commission's copy contractor, La Dorn Systems Corporation. La Dorn Systems Corporation is located in the Public Reference Room at 888 First Street, NE., Washington, DC 20426.

The Commission Issuance Posting System (CIPS), an electronic bulletin board service, also provides access to the texts of formal documents issued by the Commission. CIPS is available at no charge to the user. CIPS can be accessed over the Internet by pointing your browser to the URL address: http://www.ferc.fed.us. Select the link to CIPS. The full text of this document can be viewed, and saved, in ASCII format and an entire day's documents can be downloaded in WordPerfect 6.1 format by searching the miscellaneous file for the last seven days. CIPS also may be accessed using a personal computer with a modem by dialing 202-208-1397, if dialing locally, or 1-800-856-3920, if dialing long distance. To access CIPS, set your communications software to 19200, 14400, 12000, 9600, 7200, 4800, 2400, or 1200 bps, full duplex, no parity, 8 data bits and 1 stop bit. The full text of this order will be available on CIPS in ASCII and WordPerfect 6.1 format. CIPS user assistance is available at 202-208-2474.

TABLE OF CONTENTS

I. Introduction
II. Public Reporting Burden
III. Background
IV. Discussion
A. Open Access Issues
1. Discounting
2. Reciprocity
3. Indemnification/Liability
4. Qualifying Facilities (QF)/Real Power Loss Service
5. Right of First Refusal/Reservation of Transmission Capacity
6. Energy Imbalance Service
a. Appropriate bandwidth for small utilities
b. Settlements establishing a deviation bandwidth or minimum imbalance
7. Transmission Provider "Taking Service" Under its Tariff for Power Purchased on Behalf of Bundled Retail Customers
a. Jurisdiction
b. Purchases for retail native load
8. Indirect Unbundled Retail Transmission in Interstate Commerce
9. Mobile-Sierra
10. Tariff Issues
a. Load served "behind-the-meter."
b. Definition of "Native Load Customers."
c. Schedule changes
d. Restriction on making firm sales from designated network resources
e. Reactive Power
f. Network Operating Agreements
g. Network customers with loads and resources in multiple control areas
h. Network customer designation of load
11. Waivers of Order Nos. 888 and 889

12. Financial Independence of ISO Employees
13. Distribution Charges
14. Tight Power Pools
a. Non-pancaked rates
b. Coordination transactions
15. Legal Authority
16. Ancillary Services
17. Fair Market Value
18. Pre-Existing Transmission-Only Contracts
19. Apportionment of Transmission Revenues for Public Utility Holding Companies and Power Pools
20. Accounting for Transmission Provider's Own Use of its System
B. Stranded Cost Issues
1. Municipal Annexation
2. Pre-existing Transmission Rights
3. Load Growth and Excess Capacity
4. G&T and Distribution Cooperatives
5. Treatment of Contracts Extended or Renegotiated Without a Stranded Cost Provision
6. Customer Expectations of Continued Service at Below-Market Rates
7. Miscellaneous
V. Environment Statement
VI. Regulatory Flexibility Act Certification
VII. Information Collection Statement
VIII. Effective Date
Appendix A (List of Petitioners)
Appendix B (Tariff Revision)

I. Introduction

In this order, the Commission affirms, with certain clarifications, the fundamental calls made in Order No. 888-A.[1]

II. Public Reporting Burden

This order on rehearing issues a minor revision to Order Nos. 888 and 888-A.[2] We find, after reviewing this revision, that it does not increase or decrease the public reporting burden.

Order No. 888 contained an estimated annual public reporting burden based on the requirements of the Open Access Final Rule and the Stranded Cost Final Rule.[3] Using the burden estimate contained in Order No. 888 as a starting point, we

---

[1] As described further below, the Commission is making one revision to the *pro forma* open access transmission tariff. *See infra* section IV.A.10.f and appendix B. Because of this single revision and its minor nature, the Commission concluded that it would be administratively burdensome to require all public utilities with *pro forma* open access transmission tariffs on file with the Commission to submit compliance tariffs to reflect the revision. Accordingly, the Commission will amend all *pro forma* open access transmission tariffs currently on file with the Commission to incorporate the tariff revision and no tariff compliance filings will be necessary.

[2] Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities. Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, 61 Fed. Reg. 21.540 (May 10, 1996), *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036 (1996), *order on reh'g. Order* No. 888-A, 62 Fed. Reg. 12.274 (March 14, 1997). *FERC Statutes and Regulations* ¶ 31,048 (1997).

[3] 61 Fed. Reg. 21,540, 21,543; *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036, at p. 31,638 (1996). In Order No. 888-A, the Commission concluded that its estimate of the public reporting burden in that order on rehearing remained unchanged from its estimate in Order No. 888, 62 Fed. Reg. 12,274, 12,280; *FERC Statutes and Regulations* ¶ 31,048, at p. 30,183 (1997).

VOL. III

evaluated the public burden estimate in light of the revision contained in this order and assessed whether the estimate needed revision. We have concluded, given the minor nature of the revision, that our estimate of the public reporting burden of this order on rehearing remains unchanged from our estimate of the public reporting burden contained in Order Nos. 888 and 888-A. The Commission has conducted an internal review of this conclusion and has assured itself that there is specific, objective support for this information burden estimate. Moreover, the Commission has reviewed the collection of information required by Order Nos. 888 and 888-A, as revised and clarified by this order on rehearing, and has determined that the collection of information is necessary and conforms to the commission's plan, as described in Order Nos. 888 and 888-A, for the collection, efficient management, and use of the required information.

Persons wishing to comment on the collections of information required by Order Nos. 888 and 888-A, as modified by their order on rehearing, should direct their comments to the Desk Officer for FERC, Office of Management and Budget, Room 3019 NEOB, Washington, DC 20503, phone 202-395-3087, facsimile: 202-395-7285. Comments must be filed with the Office of Management and Budget within 30 days of Publication of this document in the *Federal Register*. Three copies of any comments filed with the Office of Management and Budget also should be sent to the following address: Ms. Lois Cashell, Secretary, Federal Energy Regulatory Commission, Room 1A, 888 First Street, NE., Washington, DC 20426. For further information, contact Michael Miller, 202-208-1415.

III. Background

In Order No. 888, the Commission required all public utilities that own, operate or control interstate transmission

facilities to offer network and point-to-point transmission services

* * * *

raised here by NEPOOL.[169] The Commission rejected NEPOOL's proposal to allow employees to possess securities of market participants as long as the value does not exceed $50,000. The Commission reaffirmed its strong commitment, set forth in Order Nos. 888 and 888-A, to ensure that an ISO is truly independent and that employees of an ISO are financially independent of market participants. However, the Commission recognized, as it had in Order No. 888-A, that there may be a need for flexibility with respect to the length of a transition period and that this matter is best addressed on a case-by-case basis.

13. Distribution Charges

NY Com seeks clarification of the Commission's statement that a utility is free to include a "distribution charge" in a customer's service agreement and/or the network customer's network operating agreement.[170] In particular, it requests that the Commission clarify that it did not intend to preempt state jurisdiction, but rather that when a term, condition or rate is required for local distribution service, the state determination will apply. It asserts that such a clarification would avoid forum shopping that would otherwise occur. In the alternative, it requests rehearing, arguing that the Federal Power Act, its legislative history and case law all dictate against Commission jurisdiction over local distribution.

---

[169] *New England Power Pool*, 79 FERC ¶ 61,374 (1997), *reh'g pending*.

[170] NY Com at 5-12.

Commission Conclusion

We clarify, as requested by NY Com, that when a term, condition or rate is required for *local* distribution service the state determination applies. We reiterate that we believe there is always a local distribution service element of a retail transaction, through which the state may impose charges on the retail customer. We also reiterate, however, that where a public utility is delivering unbundled energy to a supplier that then resells the energy to an end user, the Commission has exclusive jurisdiction over the public utility's facilities used to effect the transaction without regard to their being labeled "transmission," "distribution," or "local distribution."[171] Moreover, where a public utility is delivering unbundled energy from a third-party supplier directly to an end user the particular facts of the case will determine which of the facilities are FERC-jurisdictional transmission facilities and which are state-jurisdictional local distribution facilities.[172]

14. Tight Power Pools

a. Non-pancaked rates

NY Com seeks clarification of the following statement in Order No. 888-A:

> Order No. 888 does not require a non-pancaked rate structure unless a non-pancaked rate structure is available to pool members. Although the Commission has encouraged the industry to reform transmission pricing, the Commission's

---

[171] See Order No. 888, *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036, at p. 31,969 (appendix G) and *Allegheny Power System, Inc., et al.*, 80 FERC ¶ 61,143, at pp. 61,551-52(1997).

[172] See Order No. 888, *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036 at p. 31,969.

> current policy does not mandate a specific transmission rate structure.[[173]]

It argues that this statement conflicts with other statements that "require power pools to file joint pool-wide tariffs and to offer all transmission services that they are capable of providing."[174] NY Com asks that the Commission clarify that utility members of tight power pools must provide transmission service jointly under a single tariff. It states that this is the best way to eliminate undue discrimination. It argues that tight power pools must provide, pursuant to prior Commission orders, all transmission services that they are reasonably capable of providing and must file joint tariffs to provide transmission service on a pool-wide basis.

Commission Conclusion

NY Com appears to be confusing services that a power pool is capable of providing with *pricing methodologies* that a power pool may elect to use. While the Commission required that by December 31, 1996 all pool transactions be taken under a joint pool-wide tariff on file with the Commission, the Commission did not mandate a specific transmission rate structure for such tariff.[175] As we stated in Order No. 888-A, the primary goal for pooling arrangements is to ensure comparability regarding transmission services offered on a pool-wide basis. Thus,

---

[171] NY Com at 12.

[174] *Id.* at 13 (emphasis in original).

[175] However, as explained in Order No. 888-A, the Commission did require that all transmission rate proposals filed in compliance with Order Nos. 888 and 888-A be cost based and meet the standard *for* conforming proposals set out in the Commission's Transmission Pricing Policy Statement. *See* 18 C.F.R. § 222.

comparability is achieved if the same service is provided at the same or comparable rate to both pool and non-pool members.[176]

* * * * *

firm distinctions."[204] The Commission further noted that the appropriate treatment of revenue credits for off-system sales is dependent on the rate design used by a transmission provider and concluded that this issue is not appropriately resolved on a generic basis. Despite these identified problems, TDU Systems continues to request that the Commission adopt an automatic revenue credit mechanism without attempting to address such problems or proposing an appropriate mechanism to accomplish its request.

To bolster its proposal, TDU Systems claims that automatic treatment of revenue credits is comparable to the Commission treatment of fuel charges through the use of an automatic fuel adjustment charge. We disagree. An automatic fuel cost adjustment clause was determined to be appropriate because of the unpredictability of fuel prices.[205] TDU Systems has not demonstrated that revenue credits warrant the same treatment.[206]

---

[176] Order No. 888-A, *FERC Statutes and Regulations* ¶ 31,048, at p. 31,728.

[204] *FERC Statutes and Regulations* ¶ 31,048, at p. 30,310.

[205] *See* Treatment of Purchased Power in the Fuel Cost Adjustment Clause for Electric Utilities, *FERC Statutes and Regulations, Regulations Preambles 1982-1985* ¶ 30,524, at p. 30,800 (1983).

[206] In *Pennsylvania-New Jersey-Maryland Inter-connection, et al.*, §1 FERC ¶††††††(1997), issued concurrently with this order on rehearing, the Commission made an exception to its general approach to revenue credits and allowed monthly crediting of non-firm transmission revenues. However, this was done in the context of a major restructuring of a tight power pool.

Moreover, TDU Systems has not demonstrated that the lack of an automatic credit mechanism is likely to result in unjust and unreasonable rates. For example, the Commission's traditional means of accounting for transmission revenues for non-firm uses of the transmission system is to reflect a representative level of revenue credits (based on historical and/or projected revenue levels) in each rate case, which has the effect of lowering the transmission rate for all firm transmission users.[207] TDU Systems has not shown why a similar rate case approach to revenue credits (as opposed to an automatic credit mechanism) is not appropriate, particularly for all transmission providers. In any event, we would anticipate little or no difference between the results of an automatic revenue credit mechanism and our traditional approach and TDU Systems has not shown otherwise.

Finally, TDU Systems' proposal is one-sided in that it would only require the automatic passthrough of revenues from the *transmission provider's* use of the transmission system for offsystem sales. As the Commission stated in Order No. 888-A.

> *revenue from the transmission component of all* off-system uses of the transmission system *(whether by the transmission provider or a transmission customer)* must be treated on a comparable basis, whether through rate design or through revenue credits.[208]

---

[207] *See, e.g., Pennsylvania Power Company*, 26 FERC ¶ 61,354, at p. 61,781 (1984).

[208] *FERC Statutes and Regulations* ¶ 31,048, at p. 30,310 (emphasis added).

B. Stranded Cost Issues[209]

1. Municipal Annexation

In Order No. 888, the Commission decided that it would not be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory.[210] In Order No. 888-A, the Commission reconsidered this decision and concluded that it would be the primary forum for stranded cost recovery in a discrete set of municipal annexation cases, namely, those involving existing municipal utilities that annex retail customer service territories and, through the availability of Commission-required transmission access, use the transmission system of the annexed customers' former supplier to access new suppliers to serve the annexed load.[211]

---

[209] Some of the rehearing requests raise issues that previously were raised on rehearing of Order No. 888 and were addressed by the Commission in Order No. 888-A. The Commission will not further address such issues in this proceeding. For example, Puget repeats some of the same arguments that it raised in its request for rehearing of Order No. 888 concerning the federal causes of stranded costs, the Commission's alleged abdication of its legal authority to ensure recovery of stranded costs associated with bypass and retail wheeling, the application of the reasonable expectation test to departing retail customers, and the Commission's failure to include deferred costs in the revenues lost formula. The Commission addressed these concerns in Order No. 888-A. *See FERC Statutes and Regulations* ¶ 31,048, at pp. 30,358-62, 30,424, 30,426-27. TDU Systems reiterates its objection to the Commission's elimination of the section 35.15 prior notice of termination requirement for power sales contracts executed after July 9, 1996 that terminate by their own terms. The Commission addressed TDU Systems' concerns in this regard in Order No. 888-A. *See FERC Statutes and Regulations* ¶ 31,048, at pp. 30,392, 30,393-94.

[210] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036, at pp. 31,818.

[211] *FERC Statutes and Regulations* ¶ 31,048, at pp. 30,408-09.

A number of petitioners seek rehearing or reconsideration[212] of the Commission's decision in Order No. 888-A to be the primary forum for stranded cost recovery in the case of municipal annexations.[213] Some oppose this decision for the same reasons that they opposed the Commission's decision to be the primary forum for stranded cost recovery in the case of new municipal utilities. For example, some entities argue that the Commission does not have any authority with respect to costs in retail rate base that may be stranded as a result of the annexation of electric service territory by a municipal utility.[214] A number of petitioners also contend that municipal annexation occurs pursuant to state or local law, not federal law, and that every facet of municipal annexation, including compensation and valuation, is governed by state or local authorities.[215]

Several submit that annexation is a form of franchise competition that predated Order No. 888, that transmission access was available (though not as readily as after Order No.

---

[212] As discussed above, APPA filed its request for rehearing out-of-time. Accordingly, we are treating APPA's pleading as a motion for reconsideration.

[213] *See* APPA, CAMU, IL Com, NARUC, TAPS, TDU Systems, on the other hand, argues that the *Commission should permit non-public utilities providing reciprocal transmission service to recover* stranded costs arising from municipal annexation. TDU Systems submits that allowing public utilities to seek stranded cost recovery arising from municipal annexation exacerbates the unequal and unduly discriminatory treatment accorded transmission dependent utilities and electric cooperatives.

[214] *See* APPA at p. 11-12; IL Com at 4-5; NARUC at 2-3.

[215] *E.g.*, APPA at 12-13; NARUC at 3; TAPS at 24-25. APPA objects that federal regulation of stranded costs associated with municipal annexation results in the establishment of overlapping federal/state authority that precludes the execution of state laws by state authority in a matter normally within the power of the state, in violation of the Tenth Amendment. APPA at 13.

888) for many franchise competitors utilizing annexation,[216] and that annexations have occurred and will continue to occur based upon motivations *removed from the open access regime.*[217] CAMU states that

> [a]nnexations have occurred and will *continue to occur in a[n] unbroken string* based upon motivations entirely removed from this Commission's open access regime. There is simply no reason to assume that the Open-Access Rule will accelerate the pace of annexation.[[218]]

NARUC asks the Commission to grant rehearing as a matter of policy. It argues that the Commission's assertion of authority to address stranded cost issues related to annexation will force the Commission to inject itself into state-established processes to second-guess a state commission's cost recovery determinations. According to NARUC, this will require the Commission to resolve difficult factual issues to match specific generation and transmission facilities with specific annexed customers.[219]

CAMU similarly contends that the Commission's assertion that it is the primary forum for the resolution of annexation-related stranded cost issues will introduce needless procedural complications. CAMU submits that various state-created mechanisms exist for the identification and payment of just compensation in the case of municipal annexations. It questions how the Commission will offset against stranded cost recovery

---

[216] APPA at 11; *see also* NARUC at 3.

[217] CAMU at 2.

[218] *Id.*

[219] NARUC at 3-4.

any compensation provided under state law and whether the Commission will await the completion of state proceedings before it addresses the issue.[220] CAMU asks the Commission to defer to *existing state mechanisms and to be the primary* forum for the resolution of stranded cost recovery issues in annexation situations only where there is no state procedure for stranded cost recovery.

IL Com argues that determining whether the availability of wholesale open access is the principal cause of the stranding of public utility costs would be administratively difficult.[221] IL Com also submits that the Commission's expectation that parties raise retail-turned-wholesale stranded cost claims before this Commission in the first instance is internally inconsistent with, and contradictory to, its statements that it will give great weight in its proceedings to a state's view of what might be recoverable and will deduct any recovery a state has permitted from departing retail-turned-wholesale customers from the costs for which the utility will be allowed to seek recovery under the Rule.[222]

---

[220] CAMU at 3-5. CAMU notes that some state *compensation* statutes require the annexing municipality to pay "expectation" damages for a defined future period based upon revenues received from the annexed area. CAMU says that this element of damage, which is applied in addition to payment for condemned facilities, is meant to liquidate claims for lost service territory, idled generation assets and other business opportunities, but the awards do not separately value each of these elements of damage. CAMU questions how the Commission is going to ascertain what element of recovery pertains specifically to stranded costs if a state has adopted this liquidated damages approach. *Id.* at 5.

[221] *IL Com at 5.*

[222] *Id.* at 5-6.

Commission Conclusion

After careful consideration of the arguments raised on rehearing, we have decided not to grant rehearing, but we do provide further clarification of our decision in Order No. 888-A to be the primary forum for stranded cost recovery in certain cases involving municipal annexation. As a policy matter, we will consider recovery of stranded costs that potentially could arise as a result of municipal annexation but only when there is a sufficient nexus in such cases to the Commission's Open-Access Rule. To clarify, this determination to be the primary forum is not a blanket determination for all cases involving annexation. A determination of what circumstances make Commission review appropriate will be made on the facts pertinent to individual cases. The Commission has limited the opportunity to seek stranded cost recovery under the rule to situations in which the availability and use of wholesale open' access transmission enable a generation customer to escape a current power supplier to obtain cheaper power supplies. Annexations occur for a myriad of reasons that may have nothing to do with seeking less expensive power supplies (for example, tax or zoning considerations or consolidation of local public services). These reasons existed before adoption of Order No. 888 and, absent the nexus to the new availability of these transmission services, would not require us to consider the stranded costs from annexation in the first instance. On the other hand, an existing municipal utility that has newly-annexed territory may use an open access tariff of the annexed customers' former power supplier. Accordingly, the Commission does not believe it is necessary to reverse its previous position that annexations may raise jurisdictional stranded cost issues but instead provides this clarification.

In the course of reviewing the rehearing petitions on annexation, the Commission has also had the opportunity to reflect on the rationale for our decision to be the primary forum

for addressing the recovery of stranded costs associated with retail-turned-wholesale customers (including a newly-formed municipal utility). We wish to further elaborate upon and clarify our prior discussions about recovery of costs stranded by retail-turned-wholesale customers.[223]

First, in setting forth our position on costs stranded in certain retail-turned-wholesale and municipal annexation situations, the Commission recognized that states may also have jurisdiction over retail-turned-wholesale stranded costs and that state adjudications of such costs may precede consideration of them here.[224] Moreover, we indicated that "we are not secondguessing the states as to what a utility may recover under state law."[225] As we stated in Order No. 888-A and reiterate here.

> Our decision to be the primary forum for recovery of stranded costs from retail-turned-wholesale customers is not intended to prevent or to interfere with the authority of a state to permit any recovery from departing retail customers, such

---

[223] In so doing, we also reiterate our concern (expressed in Order Nos. 888 and 888-A) that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission—either this Commission or state commissions—to address recovery of stranded costs. *In Order Nos. 888 and 888-A,* we reserved the right to address such situations on a case-by-case basis. Order No. 888, *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036, at p. 31,819; Order No. 888-A, *FERC Statutes and Regulations* ¶ 31,048, at p. 30,409.

[224] Order No. 888. *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036, at p. 31,819; Order No. 888-A, *FERC Statutes and Regulations* ¶ 31,048, at p. 30,405.

[225] Order No. 888-A FERC *Statutes and Regulations* ¶ 31,048 at p. 30,405.

as by imposing an exit fee prior to creating the wholesale entity. [226]

In making this statement, the Commission clearly recognized that it may indeed be the states that first address the difficult stranded cost issues associated with the formation of new municipal utilities or other wholesale entities. The Commission contemplated then, as now, that it would nevertheless adjudicate those stranded cost issues where states lack authority to do so or where, based on the record before us, they fail to provide a forum,[227]

Second, as the Commission stated in Order No. 888-A.

if the state has permitted any recovery from departing retail-turned-wholesale customers (for example, if it imposed an exit fee prior to, or as a condition of, creating the wholesale entity], such amount will not be stranded for purposes of this Rule. We will deduct that amount from the costs for which the utility will be allowed to seek recover[illegible]nder this rule from the Commission.[228]

Further, we will take into account state findings on cost determinations associated with retail-turned-wholesale situations and "we will give great weight in our proceedings to a state's view of what might be recoverable."[229] We believe it is

[226] *Id.* at p. 30,410.

[227] *See City of Las Cruces, New Mexico,* SO FERC ¶ 61,160 (1997).

[228] Order No. 888-A, *FERC Statutes and Regulations* ¶ 31,048, at p. 30,405. *See also* Order No. 888, *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶ 31,036, at p. 31,819.

[229] Order No. 888-A, *FERC Statutes and Regulations* ¶ 31,048, at p. 30,405.

important to emphasize that in those instances where states do address stranded costs associated with retail-turned-wholesale customers and in cases of municipal annexation, we intend to give substantial deference to their determinations.

2. Pre-existing Transmission Rights

TAPS requests clarification that the required nexus between the availability and use of Commission-required transmission access and the stranding of costs would not be met "if the municipal utility, including as expanded through annexation, possessed rights to transmission prior to Order No. 888 and EPAct (for example, NRC license conditions and the like).[230] TAPS submits that "[t]he utility exercising these transmission rights should not be subject to stranded costs claims before the Commission simply because the municipal utility chooses to use the Commission's preferred open access tariff, instead of a bilateral or other arrangement available under pre-existing rights."[231]

Commission Conclusion

We will deny TAPS' requested clarification. The existence of rights to transmission prior to Order No. 888 would not, in and of itself, indicate that the customer should be relieved of potential stranded cost liability under Order Nos. 888 and 888-A.[232] It may be that a customer with some right to transmission

[230] TAPS at 27.

[231] *Id.*

[232] As we explained in Order No. 888-A, we declined to include "exercise of pre-existing contract rights for transmission and designation of wholesale loads" as an example of a situation for which stranded costs may not be sought because we are not prepare to make individual factual determinations in the context of the Rule. The Commission will address specific requests for stranded cost recovery on the fact presented and the merits of the particular request *FERC Statutes and Regulations* ¶ 31,048, at p. *30,358.*

service prior to Order No. 888 (for example, as a consequence of NRC license conditions), was unable to reach an alternative supplier through the use of that transmission. Thus, notwithstanding the existence of pre-existing transmission rights, and depending on the facts of a particular case, it may be that the utility incurred costs based on a reasonable expectation of continuing to serve the customer.

On this basis, the Commission will not conclusively presume that a customer with a pre-existing right to transmission service could never be subject to a stranded cost obligation under Order Nos. 888 and 888-A. Similarly, the Commission will not conclusively presume that the mere existence of a pre-existing right to transmission service precludes any reasonable expectation of continued service by the utility. However, the existence of pre-existing transmission rights, and any circumstances surrounding them, may be used as evidence in the determination of whether the utility had a reasonable expectation of continuing to serve customer.[233]

3. Load Growth and Excess Capacity

Boston Edison seeks rehearing of the Commission's finding in Order No. 88-A that "cost is not stranded if it is fully recovered the cost-based rates paid by native load."[234] submits that this phrase

> suggests that the cost of capacity released by a departing wholesale customer can and should be recovered in the rates of the remaining retail and wholesale customers if the remaining customers' load or load growth will be sufficient to absorb the released capacity . . . Such cost shifting directly

[233] *See Duquesne Light Company*, 79 FERC ¶ 61,116, at p. 61,520(1997).

[234] *FERC Statutes and Regulations* ¶ 31, 048, at p. 30,440.

> contradicts the cost responsibility principles set forth in Order No. 888 [*i.e.*, direct assignment]. [[235]]

Boston Edison objects that the rationale for this policy reversal is not articulated in Order No. 888-A.

Commission Conclusion

At the outset, we reiterate that we remain committed to the cost responsibility principle established in Order No. 888 and continue to believe that a departing wholesale customer should be responsible for the costs it stranded. Our statement that a "cost is not stranded if it is fully recovered in the cost-based rates paid by native load" was not meant to imply the cost of capacity released by a departing wholesale customer should always be recovered

[235] Boston Edison at 3.

APPENDIX G

Statutory Provisions Involved

STATUTORY PROVISIONS INVOLVED

16 U.S.C. § 824 (FPA § 201) provides in pertinent part: § 824. DECLARATION OF POLICY; APPLICATION OF PART

(a) Federal regulation of transmission and sale of electric energy

It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter [16 U.S.C. §§ 824 et seq.] and subchapter III of this chapter [16 U.S.C. §§ 825 et seq.] and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce.

(1) The provisions of this Part [16 U.S.C. §§ 824 et seq.] shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter [16 U.S.C. §§ 824 et seq.] and subchapter III of this chapter [16 U.S.C. §§ 825 et seq.], over facilities used for the generation of electric energy or over facilities used in local

distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

(2) Omitted.

(c) Electric energy in interstate commerce.

For the purpose of this subchapter [16 U.S.C. §§ 824 et seq.], electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale"

The term " sale of electric energy at wholesale" when used in this Part [16 U.S.C. §§ 824 et seq.] means a sale of electric energy to any person for resale.

(e) "Public utility" defined.

Omitted.

Federal Power Act, Section 205, 16 U.S.C. § 824d(e) (1992) provides:

Rates and Charges; Schedules; Suspension of New Rates

Sec. 205(a) All rates and charges made, demanded, or received by any public utility for or in connection with transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classification, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any public utility in any such rates, charges, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own

initiative without complaint at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and decision thereon the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate charge, classification, or service shall go into effect at the end of such period, but in case of proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f)(1) Not later than 2 years after the date of the enactment of the subsection and not less often than every 4 years thereafter,

the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine-

(A) whether or not each clause effectively provides incentives for efficient use of resources (including economical purchase and use of fuel and electric energy), and

(B) whether any such clause reflects any costs other than costs which are-

(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.

Such review may take piace in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.

(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.

(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to-

(A) modify the terms and provisions of any automatic adjustment clause, or

(B) cease any practice in connection with the clause, if such clause or practice does not result in economical purchase and use of fuel, electric energy, or other items, the cost of which is

included in any rate schedule under an automatic adjustment clause.

(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases of decreases (or both) in cost incurred by a electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

Fixing Rates and Charges; Determination of Cost of Production or Transportation

Sec. 206.(a) Whenever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate charges, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order. Any complaint or motion of the Commission to initiate a proceeding under this section shall state the change or changes to be made in the rate, charge, classification, rule, regulation, practice, or contract then in force, and the reasons for any proposed change or changes therein. If, after review of any motion or complaint and answer, the Commission shall decide to hold a hearing, it shall fix by order the time and place of such hearing and shall specify the issues to be adjudicated.

(b) Whenever the Commission institutes a proceeding under this section, the Commission shall establish a refund effective date. In the case of a proceeding instituted on complaint, the

refund effective date shall not be earlier then the date 60 days after the filing of such complaint nor later than 5 months after the expiration of such 60-day period. In the case of a proceeding instituted by the Commission on its own motion, the refund effective date shall not be earlier that the date 60 days after the publication by the Commission of notice of its intention to initiate such proceeding nor later than 5 months after the expiration of such 60-day period. Upon institution of a proceeding under this section, the Commission shall give to the decision of such proceeding the same preference as provided under section 205 of this Act and otherwise act as speedily as possible. If no final decision is rendered by the refund effective date or by the conclusion of the 180-day period commencing upon initiation of a proceeding pursuant to this section, whichever is earlier, the Commission shall state the reasons why it has failed to do so and shall state its best estimate as to when it reasonable expects to make such decision. In any proceeding under this section, the burden of proof to show that any rate, charge, classification, rule, regulation, practice, or contract is unjust, unreasonable, unduly discriminatory, or preferential shall be upon the Commission or the complainant. At the conclusion of any proceeding under this section, the Commission may order the public utility to make refunds of any amounts paid, for the period subsequent to the refund effective date through a date fifteen months after such refund effective date, in excess of those which would have been paid under the just and reasonable rate, charge, classification, rule, regulation, practice, or contract which the Commission orders to be thereafter observed and in force: Provided, That if the proceeding is not concluded within fifteen months after the refund effective date and if the Commission determines at the conclusion of the proceeding that the proceeding was not resolved within the fifteen-month period primarily because of dilatory behavior by the public utility, the Commission may order refunds of any or all amounts paid for the period subsequent to the refund effective date and prior to the conclusion of the proceeding. The refunds shall be made, with

interest, to those persons who have paid those rates or charges which are the subject of the proceeding.

(c) Notwithstanding subsection (b), in a proceeding commenced under this section involving two or more electric utility companies of a registered holding company, refunds which might otherwise be payable under subsection (b) shall not be ordered to the extent that such refunds would result from any portion of a Commission order that (1) requires a decrease in system production or transmission costs to be paid by one or more of such electric companies; and (2) is based upon a determination that the amount of such decrease should be paid through an increase in the costs to be paid by other electric utility companies of such registered holding company: Provided, That refunds, in whole or in part, may be ordered by the Commission if it determines that the registered holding company would not experience any reduction in revenues which results from an inability of an electric utility company of the holding company to recover such increase in costs for the period between the refund effective date and the effective date of the Commission's order. For purposes of this subsection, the terms "electric utility companies" and "registered holding company" shall have the same meanings as provided in the Public Utility Holding Company Act of 1935, as amended.

(d) The Commission upon its own motion, or upon the request of any State Commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

16 U.S.C. §824K(h) (FPA §212(h)) provides:

(h) PROHIBITION ON ORDERS INCONSISTENT WITH RETAIL MARKETING AREAS. – No order issued under this Act shall be conditioned upon or require the transmission of electric energy.

(1) directly to an ultimate consumer, or

(2) to, or for the benefit of, an entity if such electric energy would be sold by such entity directly to an ultimate consumer, unless

(A) such entity is a Federal power marketing agency; the Tennessee Valley Authority; a State or any political subdivision of a State (or an agency, authority, or instrumentality of a State or political subdivision); a corporation or association that has ever received a loan for the purposes of providing electric service from the Administrator of the Rural Electrification Administration under the Rural Electrification Act of 1936; a person having an obligation arising under State or local law (exclusive of an obligation arising solely from a contract entered into by such person) to provide electric service to the public; or any corporation or association which is wholly owned, directly or indirectly, by any one or more of the foregoing; and

(B) such entity was providing electric service to such ultimate consumer on the date of enactment of this subsection or would utilize transmission of distribution facilities that it owns or controls to deliver all such electric energy to such electric consumer.

Nothing in this subsection shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an ultimate consumer.

APPENDIX H

H. Rep., Hearings Before the Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce, 90th Cong., 1st Sess. (1967), excerpts from Testimony of FPC Chairman Lee C. White

H-1

FEDERAL POWER ACT AMENDMENT OF 1967

HEARINGS

BEFORE THE

SUBCOMMITTEE ON COMMUNICATIONS AND POWER

OF THE

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE HOUSE OF REPRESENTATIVES

NINETIETH CONGRESS

FIRST SESSION

ON

H.R. 5348, H.R. 5637, H.R. 7799, H.R. 8426, H.R. 8919, H.R. 9174

BILLS TO AMEND THE FEDERAL POWER ACT, AS AMENDED, IN RESPECT OF THE JURISDICTION OF THE FEDERAL POWER COMMISSION

NOVEMBER 1, 2, AND 3, 1967

SERIAL NO. 90-49

PRINTED FOR THE USE OF THE COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE

(117)

STATEMENT OF HON. LEE C. WHITE, CHAIRMAN, FEDERAL POWER COMMISSION; ACCOMPANIED BY F. STEWART BROWN, CHIEF ENGINEER, BUREAU OF POWER; RICHARD A. SOLOMON, GENERAL COUNSEL; AND DAVID J. BARDIN, ASSISTANT GENERAL COUNSEL

MR. WHITE. Thank you, Mr. Chairman. I have with me to help on any particular questions that may occur—and would like to have them sit at the table if possible—Mr. Stewart Brown, the Chief Engineer of the Federal Power Commission and the head of our Bureau of Power; Mr. Richard Solomon, the Commission's General Counsel; and Mr. David Bardin, the Assistant General Counsel who works on legislative problems for the Commission.

We at the Federal Power Commission, Mr. Chairman and other members of the subcommittee, regard this as an exceedingly important hearing. We are grateful for the opportunity to be here. I have quite a detailed statement. It would be my preference to read it. If, however, it is the preference of the chairman that we do it on a briefer basis, I can go through the highlights or present it in summary fashion.

MR. MACDONALD. Actually, Mr. White, since the proponents have been heard at length, I think it would be very well for you to read it and give us the benefit of your views on this subject.

MR. WHITE. Thank you, Mr. Chairman.

MR. MACDONALD. But I will defer to your wishes, whichever way you want to do it.

MR. WHITE. And quite obviously, even though it set up so that we hope that it flows in some logical order, it may well be appropriate and helpful if there are questions that occur for me to be stopped and we will do our best to answer those.

MR. MACDONALD. Right.

MR. WHITE. I appreciate the opportunity to present to you. Mr. Chairman and members of the committee, the views of the Federal Power Commission on H.R. 5348 and the identical companion bills. I should like to examine these bills in a somewhat broader context than their immediate effect on the regulation of the rates and accounting of interstate electric utilities. For these bills would not merely provide an exemption for certain public utilities from rate and accounting regulation by the Federal Power Commission; they would also in our view

(118)

turn back the clock on the progress the electric utility industry is now making toward lower costs and greater reliability. We therefore oppose the enactment of H.R. 5348 and I should note that this opposition to the bill is unanimous within the Commission.

These bills are before the committee today against a background of sweeping technological changes in the electric power industry. That industry is moving rapidly toward greater regional interdependence, cutting across State lines.

This trend toward greater complexity and integration has resulted in other legislative proposals, principally directed toward channeling into the most productive courses the useful progress the utility industry is making.

The proposed Electric Power Reliability Act, introduced by Chairman Staggers as H.R. 10727 and by Chairman Macdonald as H.R. 10721 represents, we believe, a realistic and constructive and constructive reaction to the changes taking place in the power industry.

Interconnections, direct and indirect, among utilities are a far more vital part of the industry's operations today than ever before, and they will be still more vital in the future. Reliability and the economies of scale newly available through use of large generators and long-distance EHV, extra-high-voltage, transmission technology demand that utilities coordinate closely, not on a local or intrastate but on a regional scale.

The Electric Power Reliability Act is intended to facilitate this broad-scale coordination. H.R. 5348 would make it, in many if not most cases, virtually impossible. We believe it would deserve the national interest to induce managements to fragment their operations and neglect opportunities to assist other systems and improve their own service by coordination with their neighbors.

We believe this would be the inevitable consequence if H.R. 5348 were enacted. The commitments the industry is now making indicate that the Electric Power Reliability Act is needed to hasten industry progress. Enactment of H.R. 5348 would in our view be a giant step backward.

WHY COORDINATION IS VITAL

The President's consumer message, transmitted February 16 of this year had the following observation and then I should like to quote from that message:

"It is becoming increasingly clear that greater coordination is needed among the various (electric) utilities to reap the benefits of reliability and economy inherent in huge generating units and extra-high-voltage transmission lines. It is also becoming evident that power systems must be carefully planned, coordinated, and strengthened to protect the consumer against cascading power failures."

The President there announced that proposed legislation would be forthcoming. In response, the Commission submitted to Congress the proposed Electric Power Reliability Act and we believe that proposal will help the power industry move toward greater cooperation and coordination.

While some elements of the industry have expressed serious doubt whether various provisions of the reliability bill will achieve their stated objectives, there has, to the best of my knowledge, been no significant disagreement with the aim of greater reliability and economy

(119)

through greater idnsitry coordination and joint planning which the bill seeks to achieve.

If I may depart from the prepared text, I have been advised that yesterday there was some discussion here before the committee to the contrary by representatives of one of the great power companies in this county.

I have not yet had a change to examine it but I may say so far as I am aware that is the first major utility to make that position. We would like to examine it and I would certainly point out to the committee that the report prepared by an industry advisory committee which was incorporated into the Federal Power Commission's report of July this year as volume 2 is quite to the contrary. It is a lengthy volume. I don't know that it would be appropriate to incorporate it in the record, but I can certainly commend it to the attention of the committee and to all who are interested in this industry.

That report was not prepared by the Federal Power Commission or its staff. It was prepared by an industry advisory committee and takes the view that I have set forth in this prepared statement.

Regional coordination is generally recognized as a national need if greater service reliability is to be realized. As the map on the easel demonstrates, cascading power failures—which do not respect State lines—have occurred in every section of the country. The Northeast blackout of November 1965 and the Middle Atlantic failure of June 1967 were the most striking examples of this kind of interruption.

To reduce the likelihood of these massive outrages, the Commission's Advisory Committee on Reliability of Electric Bulk Power Supply, the group to which I just alluded, composed of outstanding experts from all segments of the utility industry, has urged that:

The electric power industry should pursue every opportunity to accelerate the development of properly planned interconnections among individual systems.

Regional coordination among such individual systems also should be vigorously pursued since such coordination offers the most effective and economical means for assuring bulk power supply reliability for the Nation.

And further, the committee advocated:

The development of contractual arrangements to formalize the purposes, functions, organizational structure and procedures for carrying out effective regional coordination.

Thus, large-scale coordination is not an invention of the FPC which we are attempting to force on an unwilling industry. On the contrary, leaders in the utility industry, with only a few exceptions, have voluntarily committed their companies to such cooperative and interdependent action. The report of the FPC's Advisory Committee on Reliability makes clear that coordination of a type, and on a scale, utterly inconsistent with the assumptions of H.R. 5348, is needed for greater reliability in the power industry.

MR. MACDONALD. Mr. Chairman, since you asked for interruptions a question occurs.

MR. WHITE. Yes, sir.

MR. MACDONALD. Of course I agree with everything you said so far.

MR. WHITE. Yes.

(120)

MR. MACDONALD. The question that occurs is it is not what the future holds, but what the present law is, and if you could address yourself—perhaps you do later; I don't know—to the present law covering this situation I think it would be helpful.

MR. WHITE. My statement does, Mr. Chairman, get to that. By way of introduction, however, we have regarded this hearing as an excellent opportunity to in effect focus on what we regard as the other side of the coin.

I am glad indeed that some of the witnesses that you heard yesterday spoke about the impact on reliability because we believe that this is at the heart of the matter.

There are of course other aspects of it that do present themselves and we have our accounting problems, we have our financial surveillance, we have the question of rates, all of which are important, but in all candor the most important is that involving reliability in our view.

I think that I will probably touch upon that in a little more full fashion than I could otherwise do extemporaneously, but if that is agreeable I will continue.

MR. MACDONALD. Thank you.

MR. WHITE. Returning to page 5 of the text, I find it difficult to believe that the Congress of the United States would want to reject the progress of the last few years and encourage a weakening of coordination and interconnection.

HOW H.R. 5348 WOULD INHIBIT COORDINATION

The goals of adequate interconnections and sound, comprehensive contractual agreements governing coordination for reliability and economy would be far more difficult to achieve if H.R. 5348 were law.

This is so because that bill would discourage direct interconnection and full participation in interstate pools by exempting any public utility "none of whose facilities is used to transmit or receive electric energy by direct connection form or to a State other than the State in which such facilities are situated."

What is more, some utilities would be discouraged from joining reliability arrangements binding many indirectly connected utilities by the provision that the exemption shall not be available to a utility "any part of whose facilities are used to transmit or receive energy under contract with a public utility or other entity in another State."

This effect of the bill may be illustrated by the situation of the major electric utilities in the Southeastern States today. The companies in Florida have the opportunity to seek admission to a major coordination effort, the so-called CARVA-Southern

System Reliability Agreement entered into by the members of the CARVA pool, and the Southern System, a holding company controlling operating utilities in Alabama, Mississippi, Georgia, and the Florida Panhandle.

The CARVA-Southern Reliability Agreement, while undoubtedly not constituting the optimum form of regional coordination for the Southeast, represents an important and useful start in the area's progress toward regional coordination.

In all likelihood, the Florida utilities belong, as a matter of power system engineering, in this coordination group, but they have not

(121)

joined, and enactment of H.R. 5348 would certainly tend to inhibit two of them, Florida Power & Light Co. and Tampa Electric Co., from joining in the CARVA-Southern Agreement; that is, they will not "contract with a public utility * * * in another State", as H.R. 5348 phrases it, for fear of losing the promised exemption.

Even if some way could be devised to permit their participation without contracting with the out-of-State members of the agreement, the engineering efficiency of the coordination would be impaired by H.R. 5348.

Thus Florida Power & Light Co.'s service area adjoins directly that of Georgia Power Co., a participant in the CARVA-Southern Reliability Agreement, and Florida Power & Light is the largest utility in florida (and of course one of the largest in the Nation).

Yet there is no direct interconnection between Florida Power & Light and Georgia Power across the State border, and none would be likely, if H.R. 5348 were enacted, no matter how advantageous it might be operationally.

The 1964 National Power Survey report undertaken by the Federal Power Commission in cooperation with the industry and the Commission's report this year that I mentioned earlier on prevention of power failures, indicated the desirability of

stronger ties connecting the Florida utilities to the North and West. Thus the legislation before the subcommittee today would retard the progress of coordination for reliability even in the absence of reliability legislation.

NATURE OF H.R. 5348 AND RELATION TO PENDING COURT CASES

H.R. 5348 would amend the Federal Power Act to create a total exemption form parts II and III of the act for certain public utilities meeting the criteria listed by the bill.

Exactly how many companies would be exempted cannot be predicted, because of some unclear language in the bill. It is certain, however, that public utilities in many parts of the Nation could seek exemption of H.R. 5348 were enacted. The commission's report and analysis of the bill, previously submitted to the committee, discuss the language of the bill and attempt to interpret its meaning. I request that they be made part of the record and I presume that this has been previously discussed in yesterday's hearing.

We are not sure, Mr. Chairman, whether the Commission's formal report to the commerce Committee was actually discussed yesterday and made a part of the record. If it was not we believe that it would be a useful addition to the record of these hearings and so request.

(See FPC report and analysis of H.R. 5348, p.2.)

MR. BROTZMAN. Mr. Chairman, I would like to see it now. Do we have it around?

MR. WHITE. I think now, Mr. Chairman, we are approaching that portion of this prepared statement that addresses itself to the matter you raised.

In a sense H.R. 5348 may be regarded as addressed to an FPC case involving the jurisdictional status of Florida Power & Light Co. It is not my purpose here to discuss any particular case. Earlier this year the Commission concluded (two

Commissioners dissenting) that Florida Power & Light Co. is a "public utility"within the meaning of the

(122)
Federal Power Act and therefore subject to the Commission's existing jurisdiction under parts II and III of the act (37 FPC 544).

The company has petitioned for judicial review of the commissioner's decision, as is its right. Pending final disposition of the appeal, the Commission has stayed its order. In view of the pendency of the appeal obviously I cannot discuss the merits of the Commission's decision on the status of Florida Power & Light under existing law and I do not believe this subcommittee would wish me to do so.

H.R. 5348 also proposes to write into the Federal Power Act an exemption for all cooperatives financed by the Rural Electrification Administration. While such legislation was sought by most of the cooperatives of the Nation during the 89th congress, when the issue of FPC jurisdiction was pending in the so-called *Dairyland* case, that issue was resolved by the Commission, at least so far as the Commission's jurisdiction to make this determination was concerned, in an opinion earlier this year (30 FPC 365).

We held that REA co-ops are not exempt from the Federal Power Commission's jurisdiction. That matter has also been taken to the Court of Appeals in a related case, and the Commission believes that no such legislation concerning jurisdiction as it proposed in H.R. 5348 should be considered at this time.

The Commission has expressed the unanimous belief that there should be appropriate Federal regulation of generation and transmission cooperatives which transmit energy in interstate commerce, but that distribution cooperatives should not be subject to Federal Power Act regulation.

I should note that in that particular case there was one member of the Commission that dissented on the jurisdiction

over cooperatives. I think it is fair to state that with respect to the existing law it is possible for reasonable people to examine the very same fact situations, to hear the argumentation, the analysis that is set forth, and then reach conflicting views.

The way our system operates, and so far as we are concerned it is the way that it should operate, any party that is dissatisfied with a determination by the Federal Power Commission is entitled as a matter of legal right, statutory right, to appeal directly to the Court of Appeals and there contend that the Commission or a majority of that Commission was in error.

Subsequently, even if that proves to be unsatisfactory to the party, there is the opportunity to appeal to the U.S. Supreme Court. Clearly that is not the end of the route either insofar as solving a particular problem. It is the end of the route insofar as interpreting existing language.

If, however, the Supreme Court comes with a decision that is unpopular or unacceptable to a group or one individual there is then the opportunity to petition the congress to change the law, assuming that it is consistent with the Constitution.

We have here, therefore, two separate instances in which five members of the Federal Power Commission have split on the precise meaning of a section of one of the acts that we administer. We think it, therefore, perhaps would be wiser that there be no action until such time as the courts have resolved this issue or these issues.

Really there are two of them, one involving the Florida Power & Light situation and the other the co-op situation. Both of them now

(123)
are actively under judicial review and it is for this reason that we, regardless of the position that we took on the precise meaning of today's statute, believe that this legislation is at best untimely and, as my statement indicates, we believe also that is is unwise, but I hope, Mr. Chairman, I have responded to the question you have raised.

Significantly, H.R. 5348 is not being supported by the National Rural Electric Cooperative Association, an organization which did indeed support legislation in earlier Congresses to exempt co-ops expressly from certain sections of the Federal Power Act.

Nor so far as we are advised, has it been endorsed by the Edison Electric Institute, a privately owned portion of the industry, or the American Public Power Association. Also, the National Association of State Commissions is not supporting this legislation to completely exempt some utilities from the Federal Power Act.

Moreover, as my letter transmitting our report to the committee indicates, the Bureau of the Budget has advised that enactment of H.R. 5348 would not be consistent with the administration's objectives.

THE EXEMPTION PROPOSED BY H.R. 5348 IS UNWARRANTED

H.R. 5348 would exempt public utilities which transmit electric energy in interstate commerce but only through the facilities of other corporate entities and without any contractual dealings with companies in other States.

As I have indicated, any such test of jurisdiction is retrogressive in its effects upon useful interconnection and regional planning. But even in its own terms we do not believe it makes sense.

Specifically, we believe that the regulation of utilities operating in interstate commerce provided by parts II and III of the Federal Power Act is necessary and beneficial to the public and the companies.

If we are wrong, as to that, and the regulatory scheme of the Federal Power Act is obsolete or unnecessary, it should be changed or abolished across-the-board and not just with respect to companies who engage in interstate commerce in the manner prescribed by H.R. 5348.

In short we believe that would be a highly artificial distinction.

Parts II and III of the Federal Power Act were parts of the Wheeler-Rayburn Public Utility Act of 1935, enacted in recognition of legal and practical limits on unaided State action and as a corrective to widespread abuses in the power industry.

The 1935 act, therefore, placed electric utilities engaged in interstate transmission or sale of energy under Federal regulation. The act was premised on the need for a permanent system or utility regulation governing operating companies transmitting or selling energy in interstate commerce.

Let me state clearly that parts II and III of the Federal Power Act do not now apply to utilities which operate purely in intrastate commerce, in isolation form interstate networks. (By way of contract, the part IV of the Federal Power Act proposed by our Electric Power Reliability Act would include such companies, as well as the exempted Federal, cooperative, and municipal systems for the special purposes of that proposal.)

H.R. 5348 proposes to exempt from parts II and III certain additional companies which do transmit electricity in interstate com

merce. When proponents of the bill say it would exempt purely "intrastate utilities" they mean that the exempted corporations would be those owning facilities entirely within a single State, even though all or a major portion of their operations could be in interstate commerce.

The dominant rational advanced for H.R. 5348 is that it will remove from Federal jurisdiction matters concerning only the States, and allegedly so treated until recent decisions of the FPC.

However, H.R. 5348 would not have any such limited effect in our judgment. It would remove from Federal jurisdiction public utilities which sell electric energy in interstate commerce under circumstances held by the Supreme Court to give rise to Federal jurisdiction a quarter of a century ago in one of the

earliest cases decided under the Federal Power Act. This is the Jersey Central Power & Light Co., the decision by the Court in 1943.

The National Association of State Regulatory Commissions (NARUC) is not supporting the jurisdictional formula proposed by H.R. 5348. As I shall show, present FPC jurisdiction assists the States in carrying out their vital functions and H.R. 5348 would deny valuable Federal support to State regulatory programs.

Congress in 1935 believed Federal Power Act jurisdiction to be essential in three principal areas for effective regulation of electric utilities: First, wholesale sales in interstate commerce; second, financial operations and books of account; and third, interconnection and coordination of public utilities.

Congress directed the Commission to encourage voluntary interconnection and coordination, also giving it compulsory authority, upon application by a utility or a State commission, to order jurisdictional public utilities to interconnect with their facilities with other electric systems and sell or exchange energy with them.

At the same time, Congress carefully preserved the States' essential regulatory authority over matters of local import. For example, parts II and III of the Federal Power Act do not assign to the Commission any authority over retail rates; this State function covers more than 90 percent of the electric revenues of jurisdictional public utilities. States also may invoke the processes of the FPC to assure adequate interstate wholesale service.

The exemptions contemplated by H.R. 5348 could leave the Commission in the anomalous position of having jurisdiction over some investor-owned members of an interconnected network and without jurisdiction over other member of that same network.

In the same situation the small systems near the service areas of the exempt companies and the interested State commissions would have no way of seeking the Commission's help in

securing permanent interconnections and, thereby, participation in pooling on a nondiscriminatory basis, since section 202(b) of the act authorizing compulsory interconnection would no longer be available.

H.R. 5348 could exempt even utilities which were integral parts of interstate systems and even if their basic function were to generate and supply energy to out-of-state utilities as long as they did not contract directly with out-of-State entities.

Exemption could be available irrespective of the extent of the inter-state transactions engaged in, the size of the companies affected, the

(125)

number of wholesale customers dependent on them for power supply, and whether or not they were otherwise subject to wholesale rate regulation, uniform accounting, or other corporate supervisions.

In 10 States no regulatory agency would regulate the wholesales, proposed to be exempted by H.R. 5348—these are wholesales—by privately owned utilities to municipal or cooperative systems.

In any event, the engineering and financial ramifications of wholesale power transactions often extend into other States, where lack of jurisdiction and division of responsibility may make the State regulator's task impossible. It is far easier for the specialized electric rate section of the FPC to deal with the particular problem involved in wholesale rates such as firm service, emergency service, supplementary and deficiency energy, spinning reserve, reserve capacity, standby reserve, wheeling service, seasonal interchange, and economy energy.

Other difference between wholesale and retail sales concern the relationship of the parties. To a large electric utility, even a major industrial establishment is simply a retail customer. Customers who purchase power for resale, however, are often competitors, actual or potential, in the area where the two

systems are contiguous, as well as for the commercial and industrial customers.

Wholesale rate regulation raises peculiar problems which are difficult to meet in the absence of an adequate staff, expert in special wholesale rate problems.

It has sometimes been urged that compliance with the Commission's accounting requirements would be unduly burdensome and would duplicate State commission regulation. As I shall explain, we believe these arguments are based on misinformation; the experience of those utilities which now comply with FPC regulations does not support this claim.

We agree with the proponents of this legislation that "public utilities" within the meaning of the Federal Power Act are subject to accounting regulation by both the FPC and the State utility commissions.

In this respect the accounting situation differs from rate jurisdiction, where the States regulate retail sales and the FPC regulates wholesales. But as Speaker Rayburn recognized when, as chairman of this committee, he sponsored the present system in 1935, dual accounting jurisdiction strengthens both Federal and State regulation; it has generated Federal-State cooperation rather than wasteful duplication.

The system of accounts and financial reporting in general use in the State is virtually identical with that of the FPC. It is the product of joint study by State and Federal regulatory accounts. Formal interpretation of the accounting systems are closely coordinated through a joint State-Federal committee of NARUC.

Audits of individual companies' books are also coordinated. The effectiveness of our auditing program has materially helped the State commissions.

Whenever possible, joint teams of Federal and State accountants conduct audits. We also provide for State agency review of all our audits before they are made final. I have yet to see a State commission dissatisfied with the cooperative auditing arrangements wee share.

Thus, although the phrase "dual accounting jurisdiction" may at first raise questions, the practice, which is long standing now, is widely

(126)

appreciated as an effective combination of the resources of both levels of government.

It may also by appropriate to comment on a claim by Florida Power & Light Co. of the high cost of compliance with FPC regulations. The Florida Public Service Commission has required Florida Power & Light to comply with the almost identical NARUC system of accounts, identical to that of the FPC's uniform system of accounts.

The Florida commission system is now being amended to require a breakdown into units of property and continuing property records. Moreover, in 1943, the Securities and Exchange Commission acting under the Public Utility Holding Company Act, required the company to put its books on an original cost basis and to eliminate all write-ups form the company's capital accounts.

Under these circumstances we can see no basis for the claim that compliance with FPC accounting regulation by the company will be burdensome or cost anything like the sums which have been discussed in the company's testimony before the Congress.

Certainly there is no merit to the only specific claim that has been made—that the company would be required to undertake an expensive aerial survey of its facilities. We have repeatedly made clear it will have no such obligation.

In sum, therefore, the Commission urges this subcommittee to uphold the goals of the Federal Power Act by rejecting H.R. 5348. The Electric Power Reliability Act, which is also pending before the Committee on Interstate and Foreign Commerce, suggests the direction in which most of the power industry is moving, as well as the legislative response we think is appropriate.

H.R. 5348 and the other identical bills, on the other hand, would withdraw regulatory protection to which the American consumer is entitled, and hamper the power industry's progress toward better service and a more abundant supply of low-cost power for this Nation. The Commission is unanimous in judging that none of these bills be enacted.

Thank you. Mr. Chairman. That does conclude the formal statement. There is attached a copy of a map (fig.1) of the CARVA Southern System to which the statement does allude and I would hope that, too, could be incorporated into the record.

MR. MACDONALD. Without objection it is so ordered.

(The map referred to follows:)

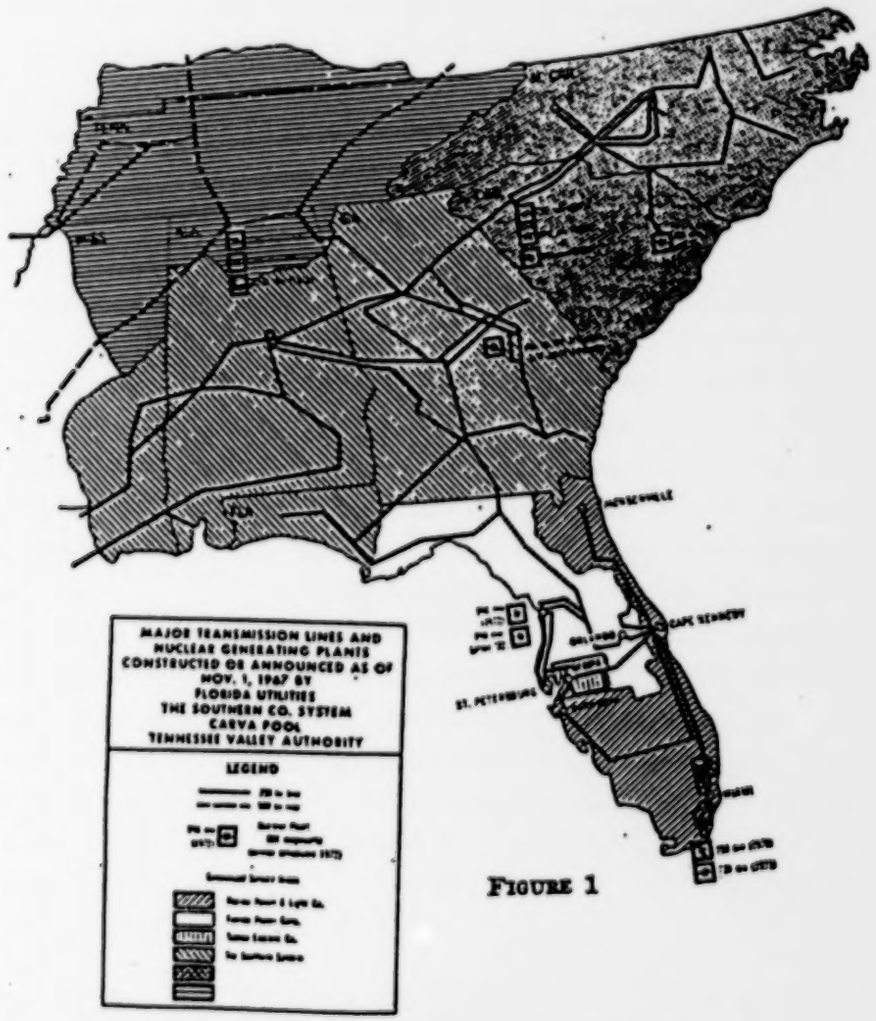


FIGURE 1

BEST AVAILABLE COPY

(127)

MR. MACDONALD. Thank your very much, Mr. Chairman. I just have two very short questions because you have answered many of the questions that have been raised yesterday and some today.

On page 7, however, I can't quite understand your statement, or at least the Florida Power & Light Co.'s position, that if this bill H.R. 5348 were enacted they would not take advantage of the operational benefits that they might have in joining up with Georgia.

Why wouldn't they want to have benefits of operation between the Georgia Power and Florida Power?

MR. WHITE. I do understand the question and I can say that it is somewhat presumptuous to make a forecast as to how any utility management will operate in the future, particularly with the way technology moves, but the way H.R. 5348 is set up if there is a utility that seeks desperately to avoid FPC jurisdiction, and there is a way that it can be done, and that way is disadvantageous to its own customers, to the need for reliable service of systems that are elsewhere in the region, we would hate to see some sort of an inducement to companies to sort of adjust their operations to the point where they can secure the exemption.

(128)

I think I should note that we have had an excellent illustration of where this has gone the other way. For a number of years the Detroit Edison Co., operated its system in such fashion that it was not jurisdictional. Within the past year or so it has concluded that, despite whatever disadvantages they may believe are inherent in FPC jurisdiction the advantages to their own system stability, to the ability to provide reliable service and economical service, are so overwhelming that they are willing to accept whatever burdens come with FPC jurisdiction, and it may well be that under circumstances that will evolve in the future even if H.R. 5348 were enacted that the management of

a particular utility would believe that it is worth the natural advantages to pay whatever psychic price or whatever financial price is involved in the FPC jurisdiction, and I could say almost in defense of the Commission we don't regard it as such a heavy burden or such a penalty.

We think there are considerable advantages that go with FPC jurisdiction. I wouldn't expect that to be a universal view, but certainly we believe, and I think that it is true, that there are many other observers of the industry, including come participants, who have seen some considerable benefit from regulation.

Only yesterday at the meeting of the National Association of State Regulatory Commissions the chairman of the Michigan Public Service Commission gave a rather powerful talk in which he said that he believed it was absolutely essential that the State commissions undertake to do more, that they had sort of left a great deal of the work to Federal agencies, and said that quite honestly he believed that if the States did not do more, if the State commissions and association did not do more, it was inevitable that the Federal Government would move in to solve national problems.

I can't say that this means that he is endorsing our electric reliability, that he is supporting this act, but his theme I thought was well taken and demonstrates that there it a vital role to be played by regulation.

MR. MACDONALD. My last question is, What is the role—I am trying to reexamine it—between the FPC and, say, the Public Utilities Commission of Massachusetts?

MR. WHITE. Under our existing legislation the State commissions including Massachusetts, are entitled to come before the FPC to allege discrimination, to seek our good offices and our procedures for resolving difficulties.

We have, I think, in the past few years seen an increasing working relationship with them. For example, in the work on our National Power Survey we have had serving on our industry advisory committee representatives of the State commissions.

We have, additionally, found ourselves cooperating with them in a lot of specific situations. The one that most recently comes to mind is the Middle Atlantic power failure of last June. We have had a joint meeting, for example, at the Federal Power Commission, meeting with the chairman of the Pennsylvania Commission, the Maryland Commission, the New Jersey Commission, the District of Columbia and the Delaware Commissions, in an effort jointly to pool whatever technical competence we have and the industry has so that our efforts will be harmonious and hopefully cumulatively better than they would be individually.

(129)

MR. MACDONALD. One of the reasons I ask is I am sure you are aware that Massachusetts has been plagued with these blackouts and Senator Edward Kennedy brought this forcefully to the attention of the Senate and at one point I thought that the FPC was about to take some steps to have the Massachusetts Public Utilities Commission take some action with the utilities in Massachusetts. I was wondering if anything ever happened in that field.

MR. WHITE. The State legislature, Mr. Chairman, set up a special committee headed by State Senator Rurich and by Representative Rorick and we have met with those gentlemen and have indicated that within the budgetary limitations of our own Commission we would indeed be glad to provide some technical competence, staff competence, to assist them.

Nothing definite has yet been worked out, but we have been in communication with then and I believe that this is an appropriate manner in which the Federal Commission can cooperate, can assist, State agencies.

MR. MACDONALD. Am I correct in assuming you can't tell the State agency what to do?

MR. WHITE. You are correct, Mr. Chairman. We do not have that authority.

MR. MACDONALD. You can merely advise and counsel.

MR. WHITE. Yes, and in all fairness I think the State commissions have been quite enthusiastic about working with us and reviewing our reports. As you may recall, we recently issued a report on the Cape Cod power failure of last summer and we have consulted with the State commission prior to the release of that.

We are hopeful that the suggestions that were contained in that report will be acted upon by the company and that if indeed they are not acted upon by the company the State commission will itself exercise whatever authority or prerogatives it possesses to achieve reliable service for the people of Cape Cod as well as elsewhere in Massachusetts.

MR. MACDONALD. I would frankly doubt that that ever comes into being, but I hope your are right. Mr. Kornegay?

MR. KORNEGAY. Thank you, Mr. Chairman. Mr. White and members of the Commission, it is certainly a pleasure to have you here with us this morning and you made a very fine statement for your position. I have a few questions I would like to ask.

Mr. White, is it your opinion, the opinion of the Commission, that it would be to the advantage of Florida Power & Light to be intertied or interconnected with Georgia companies?

MR. WHITE. I understand the question completely and it is the easiest one I am going to get all day. The answer is yes.

MR. KORNEGAY. Well, I just wanted to know because there is so much controversy about it, about that particular thing, but the reason I guess the point is controversial is, it would appear to me—just looking at the geography of it—it would be much more to the advantage of south Florida being tied in than it would be to Georgia.

They are isolated, so to speak. I really wanted to find out what your opinion is. The thing that sort of troubles me about this particular controversy, that is, assuming as you have, that it would be to the advantage of the South Florida Co. to be intertied with Georgia and

(130)

yet they are unwilling to do that because it would definitely bring there under the regulation of the FPC.

MR. WHITE. Yes, sir.

MR. KORNEGAY. Now, you have a fine commission. I am sure that the leadership of that great company is fine and all of you are dedicated to the public interest and I have no quarrel or no reason to believe otherwise.

Why would they take the position that it is a disadvantage, assuming that it is, that it is not worth whatever they have to go through to come under the regulation of the Federal Power Commission the point is that there is something wrong somewhere when reasonable men, assuming all of you see this advantage, can't get together on the procedures of the thing.

Are your rules and regulations so onerous that they outweigh the advantage they might gain by coming under the authority of the Commission?

MR. WHITE. Well, I make a claim to objectivity, Congressman but I couldn't really answer that without my biases and prejudices in favor of the Federal Power Commission procedures.

We honestly do not believe that the burdens are so onerous or ind that the burdens are not greatly outweighed by the advantages. I am in a delicate area now. I have participated in a decision in which there was a controversial issue. It was the heart of the controversy. I have taken my stand.

As you suggest, there were two other members of out five-man commission who had a different view and they are as honorable as I. I don't claim to have a greater public interest blood coursing through my veins than they have, and they reach a different conclusion.

But it is before the courts. I don't know what the court of appeals or the Supreme Court will do, but it is conceivable that they will return that case to the Commission. It is possible it could happen. If it does, I may be called upon to express an opinion a second time on it, so I want to be very careful that I

don't get myself into a position where I have prejudiced all of these issues, so I am apt to be a little delicate but I can still answer your question I think in a manner that may be satisfactory to you.

On the decision made by management—and frankly we in our reliability bill and this bill and in every public utterance by every member of the Federal Power Commission believe the responsibility must remain with management. Ownership or the control in the case of the TV they are a management just as much as the president and the board of directors of the Florida Power & Light, as are the members of the boards of the cooperatives.

They must make the decision. I believe that it is reasonable to resist regulation because you know what you have and you don't know what you might get, and we do not take it personally and we have had many people say to us, "You are five fine outstanding fellows, nothing personal, but you won't be here forever and maybe 10 years hence there will be some fellows who aren't so fine," so we try to depersonalize the matter, and I don't think this is involved, either.

But there is the natural tendency of anyone who is in the business, to resist having someone else tell him how to run his business, to look over his shoulder. I believe that is it.

(131)

MR. MACDONALD. Would you yield?

MR. KORNEGAY. Yes.

MR. MACDONALD. Actually, Mr. Chairman, I ask the president of the company—I don't think Mr. Kornegay was here when I asked him—it isn't resisting regulation really, is it, because they are regulated by the Florida Board?

MR. WHITE. Only partially, Mr. Chairman, in the sense that the Florida commission does not have jurisdiction over wholesale sales, so that is a significant factor.

MR. MACDONALD. And I would just like either an affirmative or a negative answer. The witnesses said—forget

which one, the president or the vice president of the company—said that one reason was that when they are subject to audit by the FPC they have to account for the cost of a telephone pole on Fourth Street in Miami and they say it makes it very difficult for them to make an accounting of what it costs.

They said under the State regulation they only had to account for an area.

Now, is it true that in your auditing system they have to account for what a light pole costs? I could barely believe it, although they are both very honorable men. I am not taking sides on it.

MR. WHITE. I understand the question.

MR. MACDONALD. I could hardly believe that the FPC audit would be that finite.

MR. WHITE. Our uniform system of accounts was developed with the States and in consultation with them. It is my information that the Florida Public Service Commission has recently amended its procedures to track exactly those of the FPC, or virtually exactly that of the FPC, on this matter of property inventory, so that whatever extra burdens there might have been, and I don't really believe that they are very great and I will get to that in just a moment, they are now the same, so if that might have been true 5 years ago, if our information is correct, it is not true today.

As to the cost, this was an item that was discussed and I will tell you frankly I was a little shocked when I hear that jurisdiction or nonjurisdiction might mean as much as $4 or $5 or $6 million to a company. We are not very enthusiastic about adding to the cost of an operating company. We pride ourselves, as does the industry, in trying to lower cost, and it sort of startled me and stunned me a bit to believe that it would have been at all conceivable, so I asked the chief accountant of the FPC to let me have some information: Was this accurate? Was it a rough estimate that was valid?

He came back and said he hadn't the remotest idea where the figures had come from. His estimate was, and he is physically

present in the room today, somewhere between $20,000 and $25,000 for the first year of adjustment and that it would be less after the first-year procedures had been employed.

MR. KORNEGAY. Let me interrupt, Mr. Chairman, and say if I recall the testimony not only was there the initial cost of several million but an annually recurring cost of between $500,000 and $600,000.

MR. WHITE. Those were the figures. That is correct. Those are the ones, Congressman, that shot me into our accountant's office to find out if this was accurate.

(132)

MR. MACDONALD. Isn't it a fact that even this $25,000 or $30,000 that might be charged to the company is passed on under the rules governing utilities to customers?

MR. WHITE. Yes, sir.

MR. MACDONALD. Isn't it capitalized?

MR. WHITE. Yes, sir.

MR. MACDONALD. And aren't they guaranteed a 6-percent return?

MR. WHITE. Those are operating expenses and of course are absolutely proper to be charged to the ratepayers, and we would be very sensitive indeed to be adding millions of dollars on the ratepayers' backs for something that is not required.

May I say that our chief accountant wrote a letter to the vice president of the company whose responsibility it is to come up with financial figures, offering to sit down and to discuss how we could be so far apart because it doesn't seem quite reasonable.

I have the same problem that the Congressman did, that rational human beings could find themselves in such different ball games with one in the millions and the other in the tens of thousands, and we have not yet had that meeting.

MR. MACDONALD. Thank you.

MR. WHITE. If I may, to keep this in perspective, the utilities in North Carolina and Massachusetts are paying whatever extra

cost there is. We don't think it is very great. The fact of the matter is we don't think this is so disadvantageous and the advantages might offset it and it is a net gain, but I wouldn't even make that claim. But we have not had any cries of outrage from utilities or from the State commissions who have, after all, a responsibility to see to it that the rates that their own citizens pay are as low as consistent with sound operating practice and I can't believe that a State commission wouldn't be knocking on the doors of the Congress if we were imposing such onerous burdens as a result of our regulation.

As you can tell, we do get kind of steamed up about the issue and I agree, Congressman, that on the face of it it looks kind of hard to reconcile what you have heard one day from the next day.

MR. KORNEGAY. What disturbed me was, if there were definite advantages and yesterday conscientious and dedicated people were unwilling to accept those advantages because they were saying, it seemed to me, the disadvantage was greater than the advantage they were going to receive. That was the only conclusion I could come to.

You mentioned North Carolina. As I understand it from this bill and from the prior testimony it would have no effect on any of the utilities in that State.

MR. WHITE. That is correct. My guess is if it were enacted that there would be probably no utilities in that State who would want or would be capable of adjusting their operations so as to be eligible for the exemption offered by this bill.

MR. KORNEGAY. You make reference to the CARVA pool, which composes the four utilities in the three-State area there. How is the CARVA pool working down there?

MR. WHITE. I think if you don't mind I would like to ask Mr. Brown, our chief engineer, to speak briefly to that, but generally we have seen in this country, and again not because of the wisdom of the Federal Power Commission, but because of the judgment and the

(133)
experience and the wisdom of those who operate utilities, that it makes a great deal more sense for them to coordinate and to integrate their operations so they mutually help one another. They not only afford reliable service but most of the time more economical service.

It makes good operating sense. As to how CARVA is coming along, Mr. Brown, who is our chief engineer, does work with these people in the various regions and he may have a word or two on that.

MR. F. STEWART BROWN. The CARVA pool agreement is a rather broad agreement between four of the major utilities in the Southeast and it covers the whole field of generation and transmission, the matter of interconnections, the matter of strengthening interconnections, the matter of scheduling new generation, the matter of staggering generation and being able to construct larger generations so they can share it.

It includes a consideration of reserves and the allocation of reserves among the companies. It includes the opportunity to reduce the overall reserve capability and economies and it also includes the opportunity for economic exchanges, so that we have here an opportunity for a very broad gage improvement in both the reliability and economy of all of these four systems.

MR. KORNEGAY. I believe you do have under consideration a further integration or enlarging that pool, other than a power generating company, with some who are not selling power to the public, so to speak.

MR. WHITE. Yes, in the sense that this underlies both our analysis of the past power failures and the legislation which we have pending before the committee that Chairman Macdonald introduced.

MR. KORNEGAY. That is all, Mr. Chairman.

MR. MACDONALD. Mr. Broyhill.

MR. BROYHILL. Thank you, Mr. Chairman. As the gentleman and I come from the same area in question, I would like to clear up one or two points here.

You say that in the *Florida* case, the Florida Public Service Commission, the main thing is the same system of accounts and that other States are adopting the same system of accounts that the FPC requires?

MR. WHITE. I is my understanding, congressman, that the Florida Public Service commission virtually tracks or has identical provisions although on some of the particular items these are comparatively recent actions by the Florida commission.

If it would be helpful for the record we would be delighted to submit a detailed summary of any advantages and differences.

MR. BROYHILL. I don't think that I would want that for the record, but I want to go on and say and ask if the other States are adopting the system of accounts that the FPC requires.

MR. WHITE. The answer is "Yes". I can't claim that it is 100 percent because we have some States that don't even have regulatory commissions. There are three States in the contiguous 48 that simply do not have any agencies set up for these purposes so obviously in that case it is not so.

Mr. Solomon points out that in our relationships with the States it would be better if I recast my answer to indicate that what we are talking about is not something that we have imposed or sort of pressed down on the States and that they are acquiescing and going along with it because they have no alternative.

(134)

Rather, as I tried to indicate in my formal statement and earlier, we have worked these out jointly. We have groups that meet from the State commissions and the State commissions are formed into a national association to try to develop accounting practices that are mutually beneficial.

MR. BROYHILL. What I am getting at is that under the practice today the utilities are not required to keep two or three sets of books?

MR. WHITE. That is correct and that is the purpose of this joint consultation: to establish principles that meet their needs and the Federal needs and will ease the burden on the company. We believe that if we can send our auditor together with the State auditor to the same company at the same time that it is more economical use, more efficient use, of everybody's resources, including the company's.

MR. BROYHILL. Does the Internal Revenue Service follow your system, or their own system, or what?

MR. WHITE. In terms of working with States?

MR. BORYHILL. In terms of finding out what is the net profit or gross profit before taxes.

MR. WHITE. I am not sure I quite follow the question. You mean in terms of the utilities themselves?

MR. BROYHILL. Yes.

MR. WHITE. I don't know the answer to that, to tell you the truth, I will have to check into it and find out. Our chief accountant advises, Congressman, the answer is "No; they do not."

MR. BROYHILL. Then if you come up with a figure of a total capital account the State of Florida would have that same figure as its basis for setting of rates.

MR. WHITE. To the extent that there is agreement on principles in which basic forms of rate regulation, rate setting, shall be followed, the answer would be "Yes." There could be the case in which a State would take a different view of a particular item than does the Federal Power Commission.

Our effort is to try to direct and focus attention on those areas where there are differences and which are very small and minor in terms of numbers, anyhow—they may have significance beyond the number, but for the great bulk of the accounting practices and determination to be made in accordance with a single system that we adhere to and respect and that the States accept and use for their purposes.

So it is possible we could find the Federal Power Commission reaching a different total capital cost for a utility

than would a State. We would, nevertheless, have joint audits. We would still be able to use the great bulk of those areas where our determinations are equal or equivalent.

MR. BROYHILL. If you ultimately exercise jurisdiction over the Florida Power & Light Co. this means that you will be coming in and actually telling the company how much it can charge for power or how much its rate base is?

MR. WHITE. If there were a challenge either on the initiative of a customer, on the State commission, or the FPC claiming that its wholesale rates were too high or that they were discriminatory and the FPC decided that this was a legitimate complaint that ought to be explored we could indeed find ourselves doing that just as we can for any other utility in this country that is subject to our jurisdiction.

(135)

MR. BROYHILL. You could challenge the rate on wholesale rates, but not on retail?

MR. WHITE. That is correct, and under the existing situation even the Florida Public Service Commission does not have authority over the wholesale rates charged in the State of Florida.

MR. BROYHILL. If the company does not sell any wholesale to anyone what purpose does the FPC jurisdiction serve?

MR. WHITE. If they are not selling it wholesale?

MR. BROYHILL. Yes.

MR. WHITE. Certainly with respect to rates there would be no advantage whatsoever. With respect to accounting practices, I would think there would be some benefit. It might be minimal, and if it were the case that there were no actual wholesale sales between a utility and other utilities we would have no rate problems.

There is, however, a third art of our jurisdiction that I referred to in the formal statement that had to do with the interconnections reliability of service. This is our section 202(b) of the existing Federal Power Act.

MR. BROYHILL. This is voluntary, is it not?

MR. WHITE. No, sir.

MR. BROYHILL. It is not?

MR. WHITE. No, sir. Under that, for example, we can give you an illustration. A utility in Georgia, municipally owned, claimed that it was not being adequately served by the major utilities in the area. It came to the Federal Power commission and lodged a complaint, said that its people were not being served, that they had a whole series of power failures, and "under this particular section we are seeking relief" that would not be available to a Florida municipality if I understand your question.

MR. MACDONALD. Mr. Van Deerlin?

MR. VAN DEERLIN. Thank you, Mr. Chairman. Mr. White, could you give us an estimate of the volume of power companies, not by number of companies, but I suppose by units of service provided, that would be affected by this legislation? I suppose it turns on legal interpretation of what is intrastate, but how big a slice are we talking about?

MR. WHITE. You are right, we would have to qualify any answer because first of all there is always a problem of interpreting language and some of this is kind of new and would involve both the decision within the Commission and then ultimately by the courts, by the courts, but sliding over that and the second qualifier which I think ought to be in the record, and that is you are talking I think the way things are operated today rather than were this enacted, and this is one of our fears, that there would be some companies who would undertake to adjust their operations. They may not believe it is advantageous, but they would make the decision Congressman Kornegay was talking about, that it may be worth escaping our jurisdiction if they adjust their operations.

I would think not and hope not, but to the extent that that is there we can't give you a figure. However, with those two qualifications I would say we are still talking about a pretty

small slice and maybe it is two dozen utilities in the country. It certainly wouldn't be any more than that, would be my guess.

(136)

We have not made a detailed study. It has been impossible to for reasons I have suggested. We are not talking about a large number of utilities. We are I think perhaps, however, talking about some that are quite major in the fact that they are large utilities and serve a large number of people.

MR. VAN DEERLIN. In the matter of establishing reserve margin standards, something which often imposes extra costs on a power company, what progress has been made in this direction, and establishing greater reliability, in the roughly 2 years that have elapsed since the northwest power blackout?

MR. WHITE. This is certainly one of the elements that we focused on in our preparation of our reports that came to the Congress. We have regional advisory committees established by the FPC made up of all segments of the industry in six regions of the country and we have undertaken through Mr. Brown, the head of our staff, and through our own relationships with the utility executives that serve on these committees to get them to focus on reserve factors and primarily, as your question suggested, for the purposes of reliability.

It is perfectly evident, and was in the summer of 1966 that we had one area of the country where there was just inadequate capacity. There were explanations for it. This was the St. Louis area. You may remember that persuasive heatwave that lasted for a couple of weeks and hit the whole eastern two-thirds of the country. There just was not enough power to meet all of the daily needs of the people in St. Louis and on the rotating basis the companies serving that area simply dropped loads, what we characterize as a brownout.

We had one very minor one her in the Washington area this past summer where we were operating on slightly reduced voltage in order to make sure that all the powerloads were met.

I would say we are making some progress, to answer your question, directly, and I wouldn't want to suggest that it is again our wisdom. It is the management themselves that are focusing on this. There is no utility management that wants to go through a blackout or a brownout. They grew up with service as their watchword and now they do an excellent job by and large.

MR. VAN DEERLING. Would these exemptions for the dozen, or possibly 2 dozen companies exempted by this legislation, put a crimp in this kind of planning and activity by—

MR. WHITE. It is very tempting to just give you a yes, but in fairness I must qualify it.

It would indeed under the existing legislation. If, however, the Congress acts on our electric reliability act I think the answer is it would not really have quite as much significance and may shrink down to an inconsequential area because in that proposal it is aimed at bulk power supply and does not have built within it any exemption.

That includes even the Federal operators.

MR. VAN DEERLIN. Thank you, Mr. Chairman.

MR. MACDONALD. Mr. Brown?

MR. BROWN of Ohio. Mr. White, in your statement, I would like to pursue just a couple of points and ask one question about this man.

On page 5 you suggest that this legislation would have the effect of discouraging interconnection and I presume the point that you are making is that this would reduce reliability of the individual utility, but I would put the question in another reference.

(137)

Wouldn't the discouragement of interconnection encourage the utility to have adequate power sources to meet its peak or emergency load need and, in effect, increase the reliability of that individual utility?

MR. WHITE. I understand the question completely and I must say I think that virtually all of the engineering systems and

analyses in the country, not by the Federal Power Commission but by utility managements, regardless of their form of ownership, indicate exactly to the contrary.

There is no question but what it would be possible for a system to virtually isolate its system to have adequate reserve, but in order to have that adequate reserve it has to make such a large capital investment in facilities in order to have the standby that it penalizes its own consumers by charging, legitimately charging, them more for their electric service than would otherwise be possible.

If you have one utility that is meeting its own needs it has to have another adequate reserve available instantaneously to meet any situation that can be predicted will occur within its system.

If, however, you are able to link that system A with system B then their total reserve of needs are not as great as if they were operating alone because they can move power back and forth when one has an emergency, and you don't assume that they are going to have emergencies simultaneously, so that this is the whole underlying concept for interconnection.

It is not only more reliable, but obviously cheaper. If you don't have to invest in the facilities that you will not use very often but you need them for standby or reserve purposes it makes a far better investment for the company to build transmission lines where it can move that back and forth and enter into agreements so that mutually they protect one another, so that is the answer, I believe, to your question.

MR. BROWN of Ohio. And if the assumption that both systems would not have peak demands at the same time is not correct, then when they are interconnected they are both out; is that right?

MR. WHITE. I am sorry, I think I lost you there.

MR. BROWN of Ohio. If the assumption that they will not both have peak demands or emergency demands at the same time is in error, and they should both have peak or emergency demands at the same time, then both systems are in trouble; is that right?

MR. WHITE. It depends entirely upon how well designed their reserve situation is. They will indeed be able to provide for single contingencies or even double contingencies. It is conceivable—and don't forget, now, when I am talking about these two, that is for purposes of simplification. The way it actually is working is that this is two within a group of perhaps 30 or 40.

MR. BROWN of Ohio. Like the Northeast?

MR. WHITE. Like the Northeast or, more important, like the Ohio area. Ohio now is the east-central area. We have something like 25 utilities in that region, including Michigan, Indiana, Ohio, western Pennsylvania, West Virginia, part, I think, of the tip of Maryland, and Kentucky.

Twenty-five utilities have gotten together in the reliability undertaking, so that Ohio Edison knows that if they are going to go down

(138)

they have a call on the reserve capacity of organizations that are with that, some as far away as 300 or 400 miles, and our lesson from Northeast power failure is that interconnections are bad, but that they are to be undertaken they must be strong and effective.

As we sit here today we are seeing lights operating continuously. For all we know Pepco has lost a large generator because it is tied to the PJM system. However, it has the reserve capacity of a number of systems, 11 or 12 other systems, to call upon to meet its immediate needs so that I think really it does work.

I suggest that there was testimony yesterday to indicate the contrary. So far as I know that is the first time any major utility has indicated that interconnections are somehow or other not good and ought to be discouraged. If that is the issue, then I think that these hearings are serving a highly worthwhile purpose to have attention focused on that.

MR. BROWN of Ohio. Obviously I am questioning in that area because it seems to me that it depends on how much surplus power generation capacity you have in an interconnection just as it depends on how much surplus power generation you have in an individual utility as to whether or not you can meet the emergencies that may arise, and when you tie a lot of utilities together which don't have adequate surplus power generation individually you have a lot of utilities which go down together rather than just one, and the individual utility which can meet its own needs may be able to survive in the middle of that. I rather imagine we will come to that subject in more detail at a later time, so I won't pursue it with you.

Let me move on to just pick up another point. If you can answer me very briefly on this I would appreciate it, but I did hear all the comments that were made with reference to the same line of questioning by me colleagues.

What, in addition to auditing and accounting procedures, are the added burdens of regulation by the Federal Power Commission that would make a company prefer not to be regulated by the Federal Power Commission?

MR. WHITE. That is obviously a question that perhaps someone who has different views than I could answer more forcefully, but I will do my best.

MR. BROWN of Ohio. In your testimony you suggest that there are a lot of advantages that everybody agrees to and I would imagine if somebody does not want to be regulated he may not agree to all or some of these advantages you cite.

MR. WHITE. Surely, right. I will tick them off as quickly as I can. The first is just the natural instinct not to have another group of people looking over your shoulders.

MR. BROWN of Ohio. Regulation per se.

MR. WHITE. Yes.

MR. BROWN. Of Ohio. By an additional body.

MR. WHITE. Yes. You know, you have your own situation and this introduces an unknown situation and it is perfectly rational and reasonable for somebody to resist that.

The second is that on the question of rates under the situation, for example, in Florida today there is no State agency with authority to control wholesale rates. If this Federal Power Commission has juris

(139)

diction over a particular company in Florida, as the majority of the FPC believes that it does, we will then also have the authority not only to require a accounts, but to regulate the rates that are unreasonable or that are discriminatory.

MR. BROWN of Ohio. This deals with the competitive factors to which you made reference in your testimony.

MR. WHITE. Yes.

MR. BROWN of Ohio. The factors of possible competition.

MR. WHITE. Yes.

MR. BROWN of Ohio. I want to come back to that.

MR. WHITE. Or unreasonable rates just because they are set too high or because utility. A sells to community C at one price and community D at another price and this is discriminatory. If that is the case then there is a forum where municipal C and D can come and say, "We are being discriminated against," or "Our rates are too high."

MR. BROWN of Ohio. This is not now in existence?

MR. WHITE. This is not now in existence in the State of Florida, correct.

MR. BROWN of Ohio. Are there other factors? That is two more in addition to auditing and accounting.

MR. WHITE. Yes, there is. The third one relates to this question of interconnection or compulsory linkage between two systems. Under our existing legislation, the ones that we operate under today, we have the authority wherever a public utility is jurisdictional or subject to our jurisdiction to receive complaints either from a State commission or from a utility system that says, "We are in a desperate situation and we want utility A to provide us some power, some emergency power."

MR. BROWN of Ohio. I understand that. Now, are there any others?

MR. WHITE. I don't think so. Are there any other points? They are not nearly as important to tick off as the basic ones, but also where a public utility is subject to our jurisdiction if it undertakes to acquire or merge with an additional system that must come to the FPC for approval.

MR. BROWN of Ohio. And this could in certain States be resolved by the State public utility commission, is that correct?

MR. WHITE. That is correct. An additional one is the issuance of securities by jurisdictional public utilities. If the States do not regulate that, then the Federal Power Commission under the existing Federal Power Act does regulate or have surveillance over the issuance of securities.

MR. BROWN of Ohio. But if the State does regulate it then you do not have that regulatory power.

MR. WHITE. Correct, under existing legislation, correct.

MR. BROWN of Ohio. On page 15 you make some reference to the idea that customers who purchase power for resale are often competitors (actual or potential, in the area where the two systems are contiguous) for commercial and industrial customers.

How are these competitive differences now resolved in a situation which is under your jurisdiction? Are they resolved at the State level, or the Federal level, or are they not resolved by any formal organization but rather just simply by the marketplace competition?

MR. WHITE. Under the existing authority of the Federal Power Commission if a utility contiguous to another believes and is a purchaser of power to meet its own customer needs and comes in and

(140)

claims to the Federal Power Commission, which it can do—we do have authority—that its supplier has imposed upon it restrictive provision saying, for example that it will in the

contract to supply power from A to B, that that obligation will go only so long as B does not sell to a third party at a certain volume, a competitive situation, we have had before us such a situation at the Federal Power Commission and have found that that was a restrictive provision that was contrary to public interest and have indicated we did not believe it should stand.

MR. BROWN of Ohio. Well, the reason I ask this question—I don't want to pursue it further or try to press the Chairman too far— might this not be a sixth factor in the question of whether a utility might not want to come under FPC regulation?

MR. WHITE. I thought I put that in when I spoke about rates. When we say rates we mean not only the level, but whether they are discriminatory or restrictive, so it would be a sub point of that.

MR. BROWN of Ohio. The question that I am trying to get an answer to is whether this situation is not covered in most States by State regulation? In other words, are the companies of the Federal decision in this matter where they might be more confident of the State decision in such a matter, or are the States not speaking to this problem at all?

MR. WHITE. We do have that authority where we have jurisdiction over a utility. In the States where there is no authority to regulate wholesale sales there is no place to go. There are a few such States.

Where, however, the State commissions do have authority they too can regulate them. There is a dual jurisdiction, so that there are two different forums available to the aggrieved utility who believes it is being treated harshly, unfairly, or at a great disadvantage to its customers where it might elect to go.

MR. BROWN of Ohio. Thank you.

MR. MACDONALD. Thank you, Mr. Brown. Thank you very much, Mr. Chairman, for coming here with your group. We certainly learned a good deal and it is a pleasure to once again see you up here.

MR. WHITE. We thank you, Mr. Chairman, and this has been an excellent opportunity for us to talk about some of the matters that we believe are so important.

Thank you.

MR. MACDONALD. Thank you. The next witness is Mr. H.L. Baker of the Savannah, Ga. Electric Power Co.

MR. BROWN of Ohio. Mr. Chairman, there is one point I want to make about the map before it comes down. I want to ask a question about this map because of some knowledge I have of the situation in Ohio.

Does this map only cover peak power capacity failures, or does it include technical failures, and acts of God and man and nature?

MR. WHITE. What it covers primarily, Congressman, are what we have characterized at the Federal Power Commission in our report to the Congress and the President as major power failures and those that are cascading.

MR. BROWN of Ohio. You have cities on there designated and I notice your have one in Cincinnati. I presume you indicate that is a power failure. I may be wrong.

MR. WHITE. That was not a cascading power failure, just as the one in St. Louis was not. Those are ones that were major power failures

(141)

in the sense that a large number of people were inconvenienced for a long period of time.

MR. BROWN of Ohio. The one in Cincinnati was a result of a labor dispute, was it not, or presumed to be?

MR. WHITE. There is some controversy about it. It was a case in which there was some unexplained damage to facilities and equipment.

MR. BROWN of Ohio. It was not a peak load or cascading failure.

MR. WHITE. No, sir.

MR. BROWN of Ohio. And these then include many other things besides peak load and cascading failures.

MR. WHITE. Primarily the peak load is a slightly off-beat expression for us. What we are really talking about here for the most part—underneath that overlay there is another overlay that shows the 19 major power failures that I was talking about that relate to the cascading type of failure.

MR. MACDONALD. May I interrupt, Mr. Chairman? I think this is a subject that the bill that you referred to filed by myself and Mr. Staggers would go to and doesn't really affect this particular issue and therefore I would rather not dwell on it.

MR. WHITE. All right. We do have, however, a little description of it and if it would be helpful I would send it to you, Congressman.

MR. BROWN of Ohio. All right. Thank You.

MR. MACDONALD. My last question, Mr. Chairman—and everyone has a last question—Does the FPC jurisdiction of wholesale rates come from the *Colton* decisions, so called?

MR. WHITE. It was really a decision by the Congress to vest the Power Commission with the authority and it is, I think, unambiguous and uncontroverted, so that is where it came from.

MR. MACDONALD. Thank you very much.

MR. WHITE. Yes, sir.

(The following letter was received by the committee:)

FEDERAL POWER COMMISSION
WASHINGTON, D.C., NOVEMBER 15, 1967

HON. TORBERT H. MACDONALD,
Chairman, Subcommittee on Communications and Power, House of Representatives, Committee on Interstate and Foreign Commerce, Rayburn Office Building, Washington, D.C.

DEAR CHAIRMAN MACDONALD; Thank you for your letter of November 3, 1967, asking that I develop further, for purposes of the record of the hearing on H.R. 5348, the matters

raised by your closing question concerning the Commission's jurisdiction over wholesale sales of energy by a public utility within a State to municipalities and cooperatives for distribution and resale by them. You also request that I go into the effect of the Colton case on the Commissioner's jurisdiction. I appreciate the opportunity to do so.

The Commission's jurisdiction over wholesale sales under Part II of the Federal Power Act is tied to not one but two tests, both of which must be satisfied if there is to be jurisdiction. First, the company selling at wholesale must be a "public utility" within the meaning of the Act. This statutory status now arises whenever the company engages either in transmission of electric energy in interstate commerce or in the sale of electric energy in interstate commerce for resale. H.R. 5348 proposes to change the jurisdictional tests bearing upon "public utility" status and would, as a result, exempt some companies which are now "public utilities". If a company is not a "public utility" within the meaning of the Act then none of its wholesales are subject to the regulatory provisions of Part II, and the second test is never applied. In the case of a "public utility" the Commission has jurisdiction over those wholesales which are made in interstate commerce, including sales to municipal and cooperative distribution systems for resale by them.

APPENDIX I

H. Rep., Hearings Before the Subcommittee on Interstate and Foreign Commerce, 74th Cong., 1st Sess. (1935) Frank R. McNinch, Chairman, Federal Power Commission, introducing Testimony of FPC Commissioner Clyde L. Seavey and excerpts from Seavey Testimony

I-1

Public Utility Holding Companies

HEARINGS

BEFORE

THE COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE
HOUSE OF REPRESENTATIVES

SEVENTY-FOURTH CONGRESS

FIRST SESSION

ON

H. R. 5423
TO PROVIDE FOR CONTROL IN THE PUBLIC INTEREST OF PUBLIC UTILITY HOLDING COMPANIES USING THE MAILS AND THE FACILITIES OF INTERSTATE COMMERCE, TO REGULATE THE TRANSMISSION AND SALE OF ELECTRIC ENERGY AND NATURAL GAS IN INTERSTATE AND FOREIGN COMMERCE, AND FOR OTHER PURPOSES

PART 1
FEBRUARY 19, 21, 22, 26, 28, MARCH 1, 5, 6, 7, 8, 9, 12, 13, 1935

Printed for the use of the
Committee on Interstate and Foreign Commerce

PUBLIC UTILITY HOLDING COMPANIES

THURSDAY, MARCH 7, 1935

House of Representatives,
Committee on Interstate and Foreign Commerce,
Washington, D.C.

(383) The committee met, pursuant to adjournment, at 10 a.m., Hon. William Rayburn (chairman) presiding.

STATEMENT OF COMMISSIONER FRANK R. MCNINCH, CHAIRMAN FEDERAL POWER COMMISSION

The CHAIRMAN. All right, Mr. McNinch. I think that the hearing today is specifically on title II of the bill. The representatives of the Power Commission are here.

Commissioner MCNINCH. Mr. Chairman and gentlemen of the Committee, the Federal Power Commission does feel a special degree of interest in title II of the bill under consideration because it so directly affects the functions and the jurisdiction of the Commission.

The amendments to the Federal Water Power Act begin on page 77 of the bill and the first part or title of these amendments has to do with the textual amendment for the purpose, primarily, of the clarification of the act as we now have it.

These amendments are suggested out of the experience of the Commission in its administration of the Federal Water Power Act and because of the character of these amendments, being as I have said, primarily for the purpose of clarifying the act at various places, it is thought that you may not want any extended discussion of those particular amendments; but we shall be very glad at any later time if the committee has difficulty about any one or more of those amendments to give you our views of the reasons for the necessity for such amendments.

The second part of title II, beginning at page 103, carries new matter intended to enlarge and extend the jurisdiction of the

Commission, directed primarily toward the coordination of the power generated and transmission facilities in the United States, intended as we believe, effectively, to serve the interests of the consumer in bringing to the consumers electricity upon more economical terms and at less cost than under the present lack of coordinating arrangements and likewise being equally to the interest of the companies.

This is the title that we believe there is need for some discussion on the part of the Commission in order that the committee may understand the underlying reasons or philosophy of the coordination that the Commission is suggesting.

Through this title II of title II in the bill, and because Commissioner Seavey has had such a wide and varied experience as an administrator,

* * * * *

(402) As I have indicated, it is the purpose of this bill that the Power Commission will assume only jurisdiction over the interstate wholesale business of these companies. I think I have already made that plain.

Mr. BULWINKLE. Right here, Mr. Commissioner, is where I'd like to ask you a question. You say it is the purpose of the Power Commission to only assume control over the wholesale distribution of power.

Commissioner SEAVEY. Yes.

Mr. BULWINKLE. By the Power Commission: is that correct?

Commissioner SEAVEY. Yes.

Mr. BULWINKLE. Well then taking into consideration all the provisions of this title, do you not go further than that?

Commissioner SEAVEY. With the amendments that I have indicated should be made. I do not think so.

Mr. BULWINKLE. Let us just take this proposition under section 204, providing for additions to any operating plant, noting that if that additional part, that power used, generated, from the addition were not to be used in interstate commerce,

that power plant would have to come to the Commission to ask for its approval, would you?

Commissioner SEAVEY. If it did interstate business; yes.

Mr. BULWINKLE. If it did the least interstate business?

Commissioner SEAVEY. Sir?

Mr. BULWINKLE. If it did the least interstate business it would have to come to the Commission?

Commissioner SEAVEY. Oh, yes; there is no distinction in the amount or percentage of business, interstate, that is done the utility which would bring it under the regulation of the Federal Commission.

Mr. BULWINKLE. And, you go even further than that; if the company had to give a mortgage or had any consolidations, irresponsible of what they were, under section 205, you would have control then, would you not?

Commissioner SEAVEY. Yes; those are essential provisions of proper regulation.

Mr. BULWINKLE. So the only thing that you way that you would do under this title is to provide that the States shall regulate their state charges, and the local distribution, if the company is not engaged in interstate business.

Commissioner SEAVEY. Yes; and the local services, and all the regulations regarding intrastate services and rates, and findings.

Mr. BULWINKLE. So, after we come down to it, there is very — left for any State commission, if this bill were enacted into law.

Commissioner SEAVEY. Everything is left to the State commission that they are performing now. There may be some overlapping jurisdiction as I have explained, but the States now have no jurisdiction over interstate transmission.

Mr. BULWINKLE. No; but they have over its distribution.

Commissioner SEAVEY. Yes; and under this bill, this Commission would have no jurisdiction over distribution.

Mr. BULWINKLE. I do not know whether all of the States have not; but they have control over the additions to any operating companies.

Commissioner SEAVEY. Oh, yes, sir.

(403) Mr. BULWINKLE. At the present time; but they would not under ---

Commissioner SEAVEY. Oh, yes; they would.

Mr. BULWINKLE. They would then, jointly with you.

Commissioner SEAVEY. Yes; but they would have their separate jurisdictions.

Mr. BULWINKLE. But, it could not be separate, when it is joint, would it?

Commissioner SEAVEY. Well but, the two jurisdictions will be —ted. Now, it may be that one jurisdiction might impose heavier requirements upon the utilities than the other. Those are maximum requirements.

Mr. BULWINKLE. Which commission, the State utilities commission, or the Federal Commission, would outvote the other in the joint-standard proposition?

Commissioner SEAVEY. I would say this: If a State commission proposed additional requirements for intrastate purposes upon the —ity that that would be effective. It would be beyond what the Federal Commission might impose, but they would both be effective.

Mr. BULWINKLE. But, if they did not go as far as your Commission could, then it would not be effective; your Commission would con— ?

Commissioner SEAVEY. Control so far as the maximum requirements are concerned, the same as a State commission would control as far as their maximum requirements are concerned.

Mr. BULWINKLE. I want to know for my own information—I am not trying to argue with you—but, just for my own information.

Commissioner SEAVEY. Yes.

Mr. BULWINKLE. Then, the whole title II of this title II is the regulation in the Federal Power Commission of additional power and authority, giving them the right, so far as any corporation engaged in interstate commerce is concerned for the transmission of power, no matter how little, the right to have a control over that corporation.

Commissioner SEAVEY. Yes.

Mr. BULWINKLE. That is correct?

Commissioner SEAVEY. Yes; if you are going to regulate, you must have the control.

Mr. BULWINKLE. Now, your section 209, let me just call your attention to that. Do you not think that that is a very broad section?

Commission SEAVEY. Yes, it has to be broad. You cannot regulate without the power to regulate.

Mr. BULWINKLE. There is no amendment that you will have to refer to that section?

Commissioner SEAVEY. I do not down of any to that section. That refers to the interstate practices and rules and regulations.

Mr. BULWINKLE. Will you describe to me your idea of how one of those joint boards would work?

Commissioner SEAVEY. How the joint board would work?

Mr. BULWINKLE. Yes.

Commissioner SEAVEY. I can only illustrate that by the way joint boards now work between the Interstate Commerce Commission and the State Commission of California. It is true that there has been a good deal of—

Mr. BULWINKLE (interposing). Just let me ask you right there, does the State of California Railroad or Utilities Commission nominate a (404) joint board member to work with the Interstate Commerce Commission?

Commissioner SEAVEY. Yes, sir; it appoints someone to sit with the Interstate Commerce Commission.

Mr. BULWINKLE. Someone of its own commission?

Commissioner SEAVEY. Yes: or an examiner.

Mr. BULWINKLE. But, there is no requirement in the Federal law.

Commissioner SEAVEY. Yes; there is a permission in it.

Mr. BULWINKLE. It is a permission, but not a requirement that they shall have joint boards.

Commissioner SEAVEY. There is no requirement here. It is very doubtful if you can make the requirement, where the Federal jurisdiction is concerned.

Mr. BULWINKLE. But the wording of this section is that the board shall be appointed by the Commission.

Commissioner SEAVEY. Yes.

Mr. BULWINKLE. From persons nominated by the State commission of each State.

Commissioner SEAVEY. Yes; that is positive, that the joint board would be nominated by the State commission or by the Governor, if there is no State commission.

Mr. BULWINKLE. Under the Interstate Commerce Act, your utilities or railroad commission designates one to sit with the Interstate Commerce Commission.

Commissioner SEAVEY. That is true. This goes further than that.

Mr. BULWINKLE. This goes further than that; and the Federal Government does not pay the expenses of your utility commissioner for sitting with it.

Commissioner SEAVEY. That is true.

Mr. BULWINKLE. And yet under this it does pay his per diem.

Commissioner SEAVEY. Yes: it may pay it.

Mr. BULWINKLE. So he is a Federal officer in fact, nominated by the State.

Commissioner SEAVEY. Yes.

Mr. BULWINKLE. The commission, or the Governor.

Commissioner SEAVEY. That is true. We are trying to get regulation as close to the place where it should be regulated as possible, and that is the purpose of this bill, not to take away from the States even in interstate business, a contact with the

control of the rates that must be imposed through the Federal jurisdiction.

Mr. BULWINKLE. But, while you may intend that, yet the act provides for everything that an operating company can do, says that they shall have to—engaged in interstate commerce is what I am speaking of—shall have to come to your Commission here in Washington.

Commissioner SEAVEY. Oh, yes, sir; it must come finally, if there is any conflicts, to the authority that exists.

Mr. BULWINKLE. Again, when it comes to any complaint that may be placed upon it by an operating company, before they can do that, they will have to come to the Commission in Washington, will they not?

Commissioner SEAVEY. They will have to make application, yes.

Mr. BULWINKLE. Yes.

(405) Commissioner SEAVEY. Or it might be by complaint by the States.

Mr. BULWINKLE. You are not then coming down to your local position at all.

Commissioner SEAVEY. You are getting back, you are getting federal jurisdiction back so that it will be applied as closely as possible to the locality in which it will be exerted.

Mr. BULWINKLE. Now, you are a commissioner and this question comes up to you under section 207 of legitimate prudent costs.

Commissioner SEAVEY. Might I interpose here, before we leave the other matter, that the provisions in this bill regarding joint board and cooperation are patterned after the communications bill, which this committee reported out and Congress adopted regarding the same matter. That is section 410(a).

Mr. BULWINKLE. Will you read that section?

Commissioner SEAVEY. Section 410(a), page 38 of the published — reads:

The Commission may refer any matter arising in the administration of this Act to a joint board to be composed of a member, or of an equal number of members determined by the Commission, from each of the States in which the wire or radio communication affected by or involved in the proceeding takes place or is proposed, and any board shall be vested with the same powers and be subject to the same duties and liabilities as in the case of a member of the Commission when designated by the Commission to hold a hearing as hereinbefore authorized.

Mr. BULWINKLE. Who nominates that man in the "joint board," as you call it, in the Communications Commission?

Commissioner SEAVEY. The Federal commission.

Mr. BULWINKLE. All right.

Commissioner SEAVEY. Selects him.

Mr. BULWINKLE. All right.

Commissioner SEAVEY. But, in this other act, as I stated in my explanation, we go further.

Mr. BULWINKLE. That is what I am calling your attention to, that — go further than anything we have had yet in legislation.

Commission SEAVEY. Yes: it goes further in the matter of coordinating the States and the Federal authority in complete regulation. There is not any question about that, but that this bill, as I stated, goes much further than the Communications Act, in trying to get back as far as possible to the source of the questions that may arise.

Mr. BULWINKLE. Now, let me ask you this question—

Commissioner SEAVEY: I have not completed this section.

Mr. BULWINKLE: All right, will you complete it?

Commissioner SEAVEY (reading):

The action of a joint board shall have such force and effect and its proceedings shall be conducted in such manner as the Commission shall by regulations prescribe. The joint board member or members for each State shall be nominated by the State commission of the State or by the Governor if there is no State commission, and appointed by the Federal Communications Commission.

Now, our act is broader than that.

The Commission shall have discretion to reject any nominee. Joint board members shall receive such allowances for expenses as the Commission shall provide.

Now, this act provides that when this joint board is selected, it may select a member or members to represent them and sit. There might

* * * * *

PUBLIC UTILITY HOLDING COMPANIES

FRIDAY, MARCH 8, 1935

House of Representatives,
Committee on Interstate And Foreign Commerce
Washington, D.C.

(419) The committee met pursuant to adjournment, at 10 a.m., Hon. Rayburn (chairman) presiding.

STATEMENT OF COMMISSIONER CLYDE L. SEAVEY, OR THE FEDERAL POWER COMMISSION

The CHAIRMAN. The committee will come to order. You may proceed, Mr. Seavey.

Commissioner SEAVEY. Mr. Chairman and gentlemen of the committee, I started out yesterday to try and complete my general statement, and we got into a general discussion of questions. May I proceed this morning with my general statement?

The CHAIRMAN. You may try. I think that the committee members, though, are very much interested specifically in the amendments we have to the Water Power Act. You may go ahead as far as you can.

Commissioner SEAVEY. I thought that I would endeavor to give you the general picture.

Mr. PETTENGILL. May I ask how long it would take to make your general statement, if you are uninterrupted?

Commissioner SEAVEY. Well, I presume it would take an hour, very nearly; three-quarters of an hour anyway.

Mr. BULWINKLE. I am in favor, Mr. Chairman, of letting him go ahead and complete his statement and then if we wish to we can interrogate him.

The CHAIRMAN. You may proceed.

Commissioner SEAVEY. Will the questions be limited to the same — that I take in making my statement?

Mr. PETTENGILL. There can be no assurance of that.

Mr. MAPES. A general statement without discussion of these specific amendments does not help me very much. I do not know whether it does the rest of the committee or not, but I am anxious to know what the proposed amendments are, what the effect of them is going to be.

The CHAIRMAN. Proceed.

Commissioner SEAVEY. I will try to bring that out in a general way, and then the matter of discussion of these specific provisions I thought would follow.

Mr. MAPES. In other words, the members of the committee may have some idea as to what the effect is going to be of a particular (420) amendment, and its wording and so on, and of course want to retain their right to make their own comments about that, if that —mitted.

Commissioner SEAVEY. I would say that I have personally no objection to the interjection of questions. The only objection I might have would be that I have some notes, and I do not want to stale on them before I get to the end of them.

The CHAIRMAN. Well, you may proceed.

Commissioner SEAVEY. In passing the Communications Act, I have been informed that there was under consideration the extent of the interstate calls, for instance, in telephones. At that

time on the passage of that act, that percentage was about 5 percent of the total calls.

Now, in the electrical energy field, at the present time, the movement of interstate transmission is over 17 percent. That, however, in percentage does not in either case indicate the full measurement of the need of regulation. A larger or a smaller percentage does not spell very much and that is not advanced at this time by the commission as urging that regulation is more necessary because of the larger percentage than it was in the smaller percentage, but it is interesting to note, I think, that there is a very substantial movement of interstate energy at the present time.

Mr. BULWINKLE. How much?

Commissioner SEAVEY. There is over 17 percent of the total produced moved in interstate commerce.

Of course, some of that movement may affect a very few people but the effect on those few people is just as vital to them as it was upon a much larger group of people, and so the whole field of regulation of the interstate movement is covered in this bill irrespective of the percentage that may move.

As a matter of general knowledge, however, most of this movement of interstate energy is among large groups, and to large groups. As shown by Mr. Ready in his presentation, there is now at the present time more energy moving interstate than was generated in the country in 1913.

There has been a tremendous increase not only in the total of energy generated and produced and moved in the country; but there has been a tremendous increase in the amount of interstate energy and as that increases, the problems that go with it increase so far as regulation in the States is concerned.

Mr. PETTENGILL. Well, that means then that the energy produced in 1913 was not more than 17 percent of the total energy now produced?

Commissioner SEAVEY. Yes.

Mr. PETTENGILL. In other words, in 20 years the business has multiplied nearly 500 percent.

Commissioner SEAVEY. Yes, sir.

Mr. PETTENGILL. Is there any other industry in America, outside of automobiling and petroleum, perhaps, that has moved as far as that?

Commissioner SEAVEY. I do not know, unless it is the gas industry, and I do not know that that is true with the gas. I have no figures on any other industry, but it would seem that probably there was no other industry that would show the same percentage, because of the development of the electric industry has been more tremendous, I think, in that period than either gas or other industries.

(421) Mr. PETTENGILL. Have you any idea, sir—of course it is purely a guess—as to what the industry will do in the next 20 years?

Commissioner SEAVEY. No; I am not a prophet; but I think if we look at how it has developed in the past and the potentialities of the development of its use, that there will be a tremendous increase in the development and the use of electric energy in the future. Whether that will be as much as it has been in the past formative years of the development of the energy, I would not want to prognosticate.

Mr. PETTENGILL. Well, it is nowhere near the saturation point, is it?

Commissioner SEAVEY. No.

Mr. PETTENGILL. Have you got any figures to show the percentage of individual electric energy users to the total number of people living in the areas served by these great utilities?

Commissioner SEAVEY. I do not know that I exactly understand your question.

Mr. PETTENGILL. Of course, the percentage would be much less in the rural districts, could it not?

Commissioner SEAVEY. Oh; you mean as between—

Mr. PETTENGILL. Take the number of homes in America; what percentage of them have electricity at the present time?

Commissioner SEAVEY. I could not tell you the percentage. I think I can get those figures for you.

Mr. PETTENGILL. I wish you would. Go ahead.

Commissioner SEAVEY. Now, the movement as I indicated of this interstate energy is very vital so far as the regulation of the rates and the services is concerned, especially to the States.

The United States Supreme Court has held, as I understand it, and have been informed, that a State has no control over the wholesale price of energy moved interstate.

Mr. BULWINKLE. Just right there. What percentage of this 17 percent is wholesale and what retail?

Commissioner SEAVEY. Well, I think that practically all of it is wholesale in nature. There is some that, and maybe a considerable quantity, you might call as interstate distribution; but the most of it would say was wholesale, exchange over the State lines.

Mr. PETTENGILL. Well, do the State commissions even in intrastate fix wholesale rates for that which is exchanged between one company and another?

Commission SEAVEY. Between one State and another?

Mr. PETTENGILL. No; between one company and another.

Commissioner SEAVEY. Yes.

Mr. PETTENGILL. They do?

Commissioner SEAVEY. Yes.

Mr. PETTENGILL. And between the customers and the several companies?

Commissioner SEAVEY. Yes.

Mr. PETTENGILL. All right.

Then, I would like to know how the purchaser at wholesale, interstate, suffers because the State commission has no regulation over the service or rates charged; how does he suffer?

Commissioner SEAVEY: Well, he suffers because the State has no control over the interstate energy that is sold at wholesale in his States.

APPENDIX J

New York Times, June 8, 1935,
"Utility Foes Map Floor Fight"

J-1

New York Times
Saturday, June 8, 1935
FINANCIAL 23L

UTILITY BILL FOES MAP FLOOR FIGHT

Attack on 'Death Sentence' is Expected to Win Backing in Senate Next Week.

'INTRASTATE' IS SPECIFIED

Other Amendments Accepted by Wheeler, Most of Them Restricting Its Scope.

Special to The New York Times

WASHINGTON, June 7.—Amendments to clarify the Wheeler-Rayburn Public Utility Holding Company Bill so that it specifically will not apply to intrastate business were accepted in the Senate today as the drive began to lessen the harsher provisions of the measure and to bring a final vote upon it next week.

Preceding presentation of many amendments, some adopted and others passed over, an agreement was reached to limit debate for each Senator to fifteen minutes on the bill and ten minutes on an amendment starting Monday, a program which it is hoped will assure a vote that day or Tuesday.

Before the last ballot, opponents will make two moves, one to re-commit the measure, the other to re-write Section 11, the "death sentence," down to a point where the Securities Commission, instead of killing the "unnecessary" corporations, would exercise a rigid control of all of them.

The recommittal move will, it is said, be defeated, but there are strong indications that revamping of Section 11 will be brought about.

Senator Wheeler, the bill's sponsor, offered one of the modifying amendments, providing that the Securities and Exchange Commission will exempt holding companies or subsidiaries, except where it is found that sale or distribution of securities, "by any means or instrumentality of interstate commerce,"- is detrimental to protection of investors.

Two Bailey Clauses Accepted.

In two other amendments, Mr. Wheeler agreed to protect corporations whose subsidiaries across State lines are insignificant, and to exempt companies organized in the United States but doing a foreign business.

Of forty-one amendments which Senator Bailey has offered, Senator Wheeler accepted two, considered very important by Mr. Bailey. One would permit holding companies owning stock in operating companies to purchase more stock if not against the public interest.

The other would eliminate the requirement that holding companies which registered with the Securities Commission must sign an agreement to enforce compliance with the control regulations of the commission.

Resentment against making the measure too drastic flared up on the floor when Senator McKellar told the Montana Senator that he might "get in trouble with this bill" if it was written in too severe a fashion.

The Senate, was discussing an amendment offered by Mr. Wheeler and approved, whereby the commission, instead of some outside party, would be made receiver or trustee if a court judged a utility corporation bankrupt.

This amendment, Mr. Wheeler explained, was to prevent the exercise of any "racket in bankruptcies," such as has occurred in various sections in the past.

White Exemptions Added.

Mr. Wheeler accepted an amendment by Senator White exempting corporations not primarily concerned in electric generation and supplying 75 per cent of their out put to another company. Mr. White said there were many instances of this kind in Maine.

Senator Wheeler smiled broadly when Senator Bailey proposed an extensive modification of the authority to the Federal Power Commission to determine statistics of a corporation before fixing utility rates. Mr. Bailey will presumably press the amendment on Monday.

The bill's definitions of "public utility, electric utility and holding company" were criticized by Senator White, who said:

"These definitions make it perfectly clear that any company engaged in intrastate commerce can be regulated."

Of the delegation of authority he said:

"This language lays down no statutory standard, no rules, but in the end leaves it all to the commission."

APPENDIX K

Hearings Before the Committee on Interstate and Foreign Commerce House of Representatives 74th Congress, 1st Session, (1935), excerpts from Testimony of John E. Benton, General Solicitor, NARUC

K-1

PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

HEARINGS

BEFORE THE

COMMITTEE ON INTERSTATE COMMERCE
UNITED STATES SENATE

SEVENTY-FOURTH CONGRESS

FIRST SESSION
ON

S. 1725

TO PROVIDE FOR THE CONTROL AND ELIMINATION OF PUBLIC-UTILITY HOLDING COMPANIES OPERATING, OR MARKETING SECURITIES, IN INTERSTATE AND FOREIGN COMMERCE AND THROUGH THE MAILS TO REGULATE THE TRANSMISSION AND SALE OF ELECTRIC ENERGY IN INTERSTATE COMMERCE, TO AMEND THE FEDERAL WATER POWER ACT, AND FOR OTHER PURPOSES

APRIL 16 TO 29, 1935

PRINTED FOR THE USE OF THE COMMITTEE ON INTERSTATE COMMERCE

UNITED STATES
GOVERNMENT PRINTING OFFICE
WASHINGTON : 1935

STATEMENT OF JOHN E. BENTON, GENERAL SOLICITOR, NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS, WASHINGTON, D.C.

(746) Mr. BENTON: Mr. Chairman, my name is John E. Benton. I am the general solicitor of the National Association of Railroad and Utilities Commissioners. My office is at 808 Earle Building in this city.

I have presented to the reporter certain amendments which, on behalf of the association, I request be made to the pending bill, if it shall be reported by the committee. I shall be glad if those amendments may be printed at this point, at the beginning of my statement.

The CHAIRMAN: Very well.

(The amendments referred to are as follows:)

(747) AMENDMENTS PROPOSED TO S. 1725 BY THE STATE COMMISSIONS REPRESENTED IN THE MEMBERSHIP OF THE NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS

(Words inserted are italicized. Words struck out are so shown)

AMENDMENTS TO TITLE I. BEGINNING ON PAGE 1 OF THE PRINTED BILL

At page 6 of the printed bill, amend section 2 by adding four new paragraphs, as follows:

"(d) No provision of this title shall apply to any holding company or subsidiary thereof, or public utility company which operates only in a single State under the laws of which it was organized or exists as respects any operation or business which is subject to the regulation of such State.

"(e) No public-utility company which is engaged in intrastate commerce through the rendering of intrastate utility service shall solely be reason of relationship as a subsidiary or as an

affiliate of a holding company, or of any company which is a subsidiary or an affiliate of a holding company, be held to be subject to any provision of this title.

"(f) Nothing contained in this title shall be deemed in any way to affect or to minimize the regulation and control over public-utility companies by the respective State commissions, and whenever, by the laws of any State, the State commission is given control over the issuance of securities by, or other transactions of, public-utility companies, the jurisdiction of such State commission shall be exclusive as to any matters over which it has jurisdiction.

"(g) No provision of this title shall apply to a public-utility company, the major part of the business of which is not subject to the jurisdiction of the Commission, solely by reason of the fact that such public-utility company controls another public-utility company operating in another State, the major part of the output of which, measured in volume, is transmitted to said controlling public utility, and is used by it for sale to consumers in intrastate commerce or in local distribution."

Amend the bill by striking out all of section 4(c) on pages 15 and 16 following:

"(e) ~~The Commission shall have power conditionally or unconditionally to exempt any holding company from the provisions of this section if it deems such exemption necessary or appropriate in the public interest and not detrimental to the interest of investors or consumers upon a showing that the business of such holding company and of every subsidiary company thereof is exclusively intrastate in character and confined to a single State in which such holding company and all of its subsidiary companies are organized. The Commission may, after notice and opportunity for hearing, withdraw such exemption whenever in its judgment the circumstances warrant such withdrawal.~~" .

Amend the bill at page 28 by striking out section 8 (b); following:

"(b) After January 1, 1937, it shall be unlawful for any registered holding company which, or any subsidiary company of which, is an electric utility company to own or operate, or to have any interest, directly or indirectly, through the ownership of control of securities by such holding company or any of its subsidiary companies, or otherwise, in any company which owns or operates capital assets for the transportation of natural gas in interstate commerce, or for the production of natural gas."

At page 31 of the printed bill, amend section 9 (c) to read as follows:

"(c) A registered holding company or a subsidiary company thereof may invest its funds in (1) securities of, or securities the principal or interest of which is guaranteed by, the United States, a State, a municipality or other political subdivision of a State, or any department or independent establishment of any of the foregoing or agency or corporation which is wholly owned, directly or indirectly, thereby; and (2) such other readily marketable securities, within the limitation of such amounts, as the Commission may by rules and regulations permit as appropriate for investment of current funds: *Provided, however, That nothing in this Act shall exempt any public utility company from obedience to the law of any State within which it operates.*"

At page 57, amend section 15 (e) to read as follows:

"(e) After the Commission having jurisdiction thereof has prescribed the form and manner of making and keeping accounts, cost-accounting procedures, correspondence, memoranda, papers, books, and other records to be kept by any company hereunder, it shall be unlawful for any such company to keep any accounts, cost-accounting procedures, correspondence, memoranda, papers, books, or other records other than those prescribed or such as may be approved by the Commission having jurisdiction thereof, or to keep its accounts, cost-

* * * * *

(760) Mr. BENTON: Mr. Chairman, I recognize the difficulty of securing the attendance of members of the committee when the Senate is in session.

The CHAIRMAN: You may proceed.

STATEMENT OF JOHN E. BENTON, GENERAL SOLICITOR, NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS, WASHINGTON, D.C.—Resumed.

Mr. BENTON: Mr. Chairman, before the recess I was saying that the State commissioners felt that legislation enacted by the Congress with respect to holding companies should be confined to holding companies which operate outside the States where they are organized.

A State is competent to control the operations of holding corporations and of public-utility companies created by it and operating wholly within its own borders. No interstate-commerce feature is involved in the operations of such companies; and the evils described in section 2 do not arise from those operations. We ask that such intrastate companies be altogether excluded from the scope of the bill.

We ask also that the holding company title portion of the bill be confined in its effect to holding companies, and that no public utility be subjected to regulation under the holding company section solely by reason of its relationship as a subsidiary or an affiliate of a holding company. Whatever regulation Congress deems proper to impose on electric utilities we ask to have included in title II of the bill which ostensibly relates to them.

While the State commissions favor Federal regulation of the wholesale transactions of electric utilities, they urge that the legislation should go no further than is necessary to protect the public interest in this field which is beyond the reach of State regulation.

The amendments which we have presented to title II accordingly are designed to limit the jurisdiction to be conferred

by Congress upon the regulating Federal commission to the regulation of wholesale transactions where electric energy is purchased at wholesale for ultimate resale to the consuming public.

Before taking up the amendments, I wish to say this: It may appear that we have been over-meticulous and repetitive in the provisions which we have asked Congress to insert for the preservation and protection of State powers. However, the State commissions have learned from bitter experience that too great care cannot be taken in this respect.

When Congress passed the act to regulate commerce in 1887, it placed in the first section of that act this seemingly explicit provision:

Provided, however, That the provisions of this Act shall not apply to the transportation of passengers or property, or to the receiving, delivering, storage, or handling of property, wholly within one State, and not shipped to or from a foreign country from or to any State or Territory as aforesaid.

Yet, notwithstanding that declaration, a provision in the third section of the act forbidding discrimination against persons or places, was construed to give the Interstate Commerce Commission the power over intrastate rates, which was exercised in the *Shreveport case*, and today State jurisdiction has become not much more than a shadow in the railroad field. The State commissions do not wish to repeat that experience in the utility field. Accordingly, they have sought in, (761) the amendments offered to title II of this bill to separate the field within which the Federal regulatory commission may exercise jurisdiction from that which is reserved to the States, and to make that separation so clear and explicit throughout the bill that there may be no opportunity for judicial construction to make the legislative purpose miscarry.

Mr. CHAIRMAN, at this point I take up the *Pennsylvania Gas Co. case*, and some other cases. Without reading that portion of

my statement if it may be made a part of the record I will pass on.

The CHAIRMAN: Very well.

Mr. BENTON: You will notice that in the resolution adopted at our annual convention in 1929, the Congress was asked not to invade the field of local service, but to leave that field to the State authorities. The position then taken by the association has been consistently maintained ever since. And in that resolution the *Pennsylvania Gas Co. case* (252 U. S. 23, 30) is cited. That is the case in which the United States Supreme Court held that the Public Service Commission of New York could regulate the rate for gas sold to local consumers in New York, although the company selling it produced the gas in Pennsylvania and delivered the same across the State line to the customers in New York. The Court in its opinion said:

The rates of gas companies transmitting gas in interstate commerce are not only not regulated by Congress, but the Interstate Commerce Act expressly withholds the subject from Federal control * * * The thing which the State commission has undertaken to regulate, while part of an interstate transmission is local in its nature and pertains to the furnishing of natural gas to local consumers within the city of Jamestown, in the State of New York. The pipes which reach the customers served are supplied with gas directly from the main of the company which brings it into the State; nevertheless, the service rendered is essentially local, and the sale of gas is by the company to local consumers, who are reached by the use of the streets of the city in which the pipes are laid, and through which the gas is conducted to factories and residences as it is required for use. The service is similar to that of a local plant furnishing as to consumers in a city. This local service is not of that character which requires general and uniform regulation of rates by congressional action, and which has always been held beyond the power of the States, although Congress has not legislated upon the subject. While the manner in which the business is conducted

is part of interstate commerce, its regulation in the distribution of gas to local consumers is required in the public interest, and has not been attempted under the superior authority of Congress. It may be conceded that the local rates may effect the interstate business of the company. But this fact does not prevent the State from making local regulations of a reasonable character. Such regulations are always subject to the exercise of authority by Congress, enabling it to exert its superior power under the commerce clause of the Constitution.

It was said before the House committee that the *Pennsylvania Gas Co. case* has been overruled in *East Ohio Gas Co. v. Tax Commission* (283 U. S. 465). It was not overruled on the point now under discussion. The *East Ohio Gas Co. case* was a tax case. The State of Ohio had levied an excise tax upon the gross receipts of gas utilities from sales to consumers. The East Ohio Co. sought to enjoin the collection of the tax upon the ground that its gas in large part was brought into Ohio from other States. The company depended upon the well-established principle that a State may not tax the proceeds of interstate business. If the sale to consumers of the gas brought into Ohio by the distributing company was interstate commerce, the tax was invalid. It was accordingly necessary for the court to hold the sales intrastate to sustain the tax.

(762) The company cited the *Pennsylvania Gas Co. case* to establish the interstate character of the commerce, the court in that case having said that what was dealt with there was interstate commerce.

In the *Ohio case* the court held that, under circumstances shown in the record in the *Ohio case*, the sales to consumers were intrastate in character. The court ruled that after gas had been brought into the State under pressure, and then the pressure had been reduced for the purpose of enabling distribution to consumers, the stepping down in the pressure of the gas marked the end of interstate commerce, and that all that took place thereafter was intrastate commerce. The court disposed of the

Pennsylvania Gas Co. case by saying that it did not appear that the point upon which the *Ohio case* was determined was presented to the court in the *Pennsylvania case*, but that if it was presented the case was disapproved to the extent in conflict with the decision made in the *Ohio case*. I quote from the opinion the exact language used:

It does not appear that there were presented in *Pennsylvania Gas Co. v. Public Service Commission*, to the State court or where the considerations on which it is held that interstate commerce _____ over intrastate business begins when gas flowing through pipe lines from outside the State passes into local distribution systems for delivery to consumers in the municipalities served. But, however that may be, the opinion in the *Ohio case* be disapproved to the extent that it is in conflict with our decision here.

This decision accordingly in no way whatever conflicts with the principle discussed and applied in the *Pennsylvania Gas Co. case*, which was that being to consumers, even though made in interstate commerce, are local to their character and subject to State regulation so long as Congress does not destroy the field.

That this was the point deemed in the *Pennsylvania case* and that the decision rested on that point as shown by the following language from the opinion of Mr. Justice Sutherland in *Barrett v. Kansas Natural Gas Co.* (289 U. S. 298-308).

There the Gas Co., a Pennsylvania corporation, transmitted gas from Pennsylvania into New York and sold it directly to the consumers. The service to the consumers, which was the thing for which the requested charge was made, was essentially local, and the decision rests upon this nature.

The CHAIRMAN: Isn't it true, that all States do not have commissions with full jurisdiction in the matter of regulatory powers over all activities of public utilities.

Mr. BENTON: There are a few which have not.

The CHAIRMAN: (continuing). In many States the regulatory commissions are limited to certain specific things, and their powers are not broad enough to cover really a full investigation of the public utilities.

Mr. BENTON: Perhaps that is an overstatement. I do not think that is true of many of them.

The CHAIRMAN: As I stated this morning, for instance some legislatures have hampered their commissions by not giving them sufficient funds to carry on their investigations to the point where they can really render a public service.

Mr. BENTON: It is true as you state, Mr. Chairman, that in some States the appropriations are inadequate. That is another aspect of the matter, not covered by this bill.

(763) Of course, the amount of service of this local character which passes over State lines, is not very great. The question arises whether for the sake of supplying regulation which has not as yet been supplied for service to the comparatively few people who would obtain it, if you should pass an act going to the full limit that Congress could go in the exercise of its constitutional powers; you should enact a bill which would break down the regulatory powers of the many States which have provided their people with local commissions, which for the most part are reasonably well financed, and are effectively regulating the local service in those States.

The CHAIRMAN: Do you not think there is a general feeling in this country to the effect that the local utility commissions have not done a very satisfactory job with reference to rates charged by utility companies?

Mr. BENTON: Personally I do not think so. I do think that you now and then find allegations of that sort made, but in my own judgment, since you have asked the question, that feeling is not very general. It is not very generally believed that the local regulatory commissions have not done a good job.

At least, I flatter myself that that was not the feeling in the State of New Hampshire, when I was honored by being a commissioner there. I know that that was not the feeling when

Senator Brown was acting as a commissioner in New Hampshire. And I do not believe it is the feeling in the State of Indiana, where Senator Mintou at one time was counsel for the commission. In my judgment that is not true generally.

I do not mean to say that in the 48 States—or inasmuch as Delaware does not have a State commission I will say in the 47 States—that you always have in those 47 States well chosen commissioners who are acting as effectively as they should act. But I think you are getting in the regulatory field as good service as the people are entitled to. If the people are taking an interest in seeing that they are well served by their officials, then they are well served. If they go to sleep and allow individual commissioners to get elected or appointed who neglect their duties, then it may happen in such instance that the commission may not give good service—I do not think it is happening generally.

Senator BROWN: Is not a great deal of the trouble the matter of getting enough money out of the legislature? That is; they give their commission authority enough but do not give them money enough to work with. Do you think that is more or less general?

Mr. BENTON: I think it is true, especially since the depression, that appropriations have been cut below what they ought to have been cut. At the same time there is a movement going on to increase appropriations. Some of our commissions are better supplied with funds today than ever before since their creation. There is a very considerable movement to place the cost of public service regulation upon the regulated utilities; by means of some form of direct assessment of the cost upon the utilities, which in the end of course is borne by the people who receive the service and pay for it. If the service is worth what it costs, the people who get the benefit of it properly pay for it in the end.

The CHAIRMAN: This bill expressly provides that local rates shall be determined by the State commissions, does it not?

(764) Mr. BENTON: Yes. It is designed to do that, and we recognize—

The CHAIRMAN: (interposing). Why should a State commission object to having the Federal Government get information and turn it over to them?

Mr. BENTON: They do not.

The CHAIRMAN: That is, provided they themselves are the ones who are going to finally determine what the rates shall be.

Mr. BENTON: I do not think they should object. And the association for which I speak not only does not object, but it ask the Congress to enact that kind of legislation. As a matter of fact our association, I think some 3 years ago, passed a resolution asking the Congress to set up a commission to do exactly that sort of thing.

The CHAIRMAN: This bill also provides for joint boards. That is, the bill provides that the commission may appoint joint boards to take up matters with the local commissions in the States where a matter affects them.

Mr. BENTON: I know it does that. It is the same sort of provision that you put into the Communications Act. We think it is very helpful. We recognize that the purpose of this bill is to bring about improvement in the law, to bring about the reforms which are necessary in the public interest, and that we approve. But we are desirous that the Congress in doing that shall not inadvertently so draw the law as to break down the local regulatory agencies.

The CHAIRMAN: I do not think there is any intention to break down the local regulatory bodies. On the contrary, I think the drafters of the bill intended to strengthen the State commissions.

Mr. BENTON: I believe that is true. I am now speaking about section 2. I am unable to see how title I could have been drawn by anyone who was very solicitous for the preservation of the powers of the local regulatory agencies. I had some discussion about title II with members of the Federal Power Commission, who I assume aided you in drawing the bill, and I know that—

The CHAIRMAN: (interposing). They did more than aid me. [Laughter.]

Mr. BENTON: I am perfectly certain that the members of the Federal Power Commission desired to see the regulatory powers of the State commissions preserved. Yet there are certain provisions in the bill which, if they were enacted just as they now stand, would be very destructive of State powers, as I think I shall be able to point out to you as I go along.

The CHAIRMAN: All right. You may proceed.

Senator BROWN: Mr. Benton, take the case of a fly-by-night promotion company that buys up 6 or 7 or 8 small gas, electric, and waterworks companies, with an engineer in charge in the State but who has no authority except to look out for the plant, and the president or the vice president of the company is located, say, in New York, or at least out of the State, how is the State commission going to regulate that situation, particularly when the president, we will say, who is in New York, which is outside the State, has an office beyond your jurisdiction, and when you call his office they say he is at his residence, and if you call his residence they say he is at his office, and they keep you running back and forth for a period of months, just how are you going to get at that matter?

(765) Mr. BENTON: That is the kind of situation which, as I have said, our association thinks the Congress should take care of by Federal regulation because the States—

Senator BROWN: (interposing). That is an entirely intrastate operation so far as the companies are concerned.

Mr. BENTON: As to the operating company itself, of course the local commission would have no trouble in regulating it. But the operations of the holding company in New York the State commission cannot regulate.

Senator BROWN: I do not know whether the State can regulate that situation even. For instance, these men who are in the plant have no authority, have no figures, and I am just assuming that you have a set of men who are not amenable to regulation; what are you going to do about it?

Mr. BENTON: I see what you are talking about now, I think. You are asking me the question: How is the State going to

regulate that local utility intelligently when the men who are operating the utility in New Hampshire are not the responsible people who direct the actions of the company, and do not have the information that the local utility commission needs in order to make its orders intelligently?

Senator BROWN: They know nothing about it.

Mr. BENTON: That is exactly the situation where the State is impotent. But it will not be impotent if the Congress creates a commission which has full regulatory power over the holding company, and may require the holding company to keep its books in an understandable manner, which will place the information the State commission needs in the hands of the States commission.

The CHAIRMAN: That is exactly what this bill proposes to do.

The BENTON: And that is exactly what we are here saying we think you ought to provide for by an act of Congress.

The CHAIRMAN: All right.

Mr. BENTON: I started, Mr. Chairman, to read a quotation from the *Pennsylvania Gas Co. case*, following with some further discussion and citations, but I believe it was agreed that that may go into your record without reading.

The CHAIRMAN: That is understood.

Mr. BENTON: At our last convention, held in November 1934, the legislation which is now before us was being talked about. It was understood to be in course of preparation. There was very genuine alarm among State commissioners lest the legislation should be in such form that State powers would be annihilated, as they were in the railroad field; and a resolution of protest was presented to the executive committee. This resolution was redrafted and adopted. The redrafting was to make acknowledgment of the helpful attitude of the administration of which Congress is so large a part in its action on the Communications Act and on the Johnson bill, in extending protection to the local State authorities. The resolution, however, reaffirmed the stand of the association taken in 1929. I will read the resolution, as follows:

While we appreciate the aid given to our representatives during the year by the national administration in protecting the rights of the State regulatory bodies and aid helped spirit of many officials engaged in the Federal field where there is joint interest and jurisdiction, and while we recognize the need of cooperation on the part of State regulatory bodies where there is such joint interest and jurisdiction, we are of the opinion that there is a possibility of unnecessary attempts (766) to assume or acquire jurisdiction by the Federal Government or some branch thereof in the field of purely local or State regulation and police power.

Be it therefore resolved, That this association reiterates its stand taken in previous years in the passage of various resolutions in relation thereto, to the effect that the association is opposed to any encroachment upon the regulatory jurisdiction of the States, as not being compatible with the local public interest which can best be served through agendas chosen by those whom existing problems affect.

In setting up the National Power Policy Committee the President gave voice to the principle which we have asked the Congress to apply, and in speaking of legislation to be enacted by the Congress he said:

Since a number of the States have commissions having jurisdiction over intrastate power matters, it is necessary that whatever plan is developed should have regard to the powers of these various State commissions as well as of the States in general.

Our appearance here is to renew our acknowledgment and our expressions of appreciation of the disposition which has been shown by the Congress and by the President to preserve the local agencies, which the States have created for the protection of their people, from being disabled or broken down, and to point out to the committee respects in which we think this bill must be

amended to bring it into harmony with the purpose of the President and the Congress to preserve and strengthen these local agencies.

The association approves Federal legislation for the regulation of holding companies, and of wholesale transmission and sale of electric energy and gas. As I have already said; the association favors well-considered Federal legislation which will end the evils and abuses now known to result from holding-company operations, and which shall provide for the regulation of the wholesale transmission and sale of electric energy.

I do not mean to say that there is absolute agreement with respect to this legislation among the 47 commissions represented in our association. Such agreement would not be expected concerning a bill which has aroused so much apprehension and controversy as the pending bill has aroused. The bill has, however, received intense committee consideration, and the position now taken by the association has been carefully formulated. I shall state to you the manner in which the bill has been considered and the action taken thereon and the manner in which the several commissions have been kept advised concerning that action; and I shall present to you such expressions of dissent as have been received from any commission.

Holding companies escape the reach of State authorities when they operate outside the State in which organized. It is for this reason that the association favors Federal legislation, provided it is so drawn as to apply only to interstate holding companies.

It is evident that a State commission cannot reach beyond the borders of the State to investigate, to call witnesses, and to control corporate acts. Even when a commission can secure evidence which satisfies it that holding-company control is being used to impose improper costs upon an operating utility subject to its jurisdiction, it is nevertheless restricted in its action and powers.

In the *Southwestern Bell Telephone Co. case* 262, U.S. 276; the United States Supreme Court had before it an order of the

Missouri commission reducing telephone rates. The order was based in part upon a (767) finding by the Missouri commission that the service contract between the Southwestern Bell and its parent company, the A.T.&T., under which the subsidiary paid to the parent company 41/2 percent of its gross revenues for certain financial and other services provided by the holding company through its New York office, resulted in overpayment for those services, and in an overstatement of operating expenses. The court overturned, that over, upon the ground, among others, that the commission had no right to go into that contract, because that was an invasion of the field of management.

I want to read the portion of the opinion dealing with that service contract because, while the ruling has been in part by implication overruled since Mr. Hughes because Chief Justice, it has been so overruled only in part.

In the *Southwestern Bell case* the Court said:

Four and one-half percent is the ordinary charge paid voluntarily by local companies of the general system. There is nothing to indicate bad faith. So far as appears, plaintiff in-error's board of directors has exercised a proper discretion about this matter requiring business judgment. It must never be forgotten that while the State may regulate, with a view to enforcing reasonable rates and charges, it is not the owner of the property of public-utility companies, and is not clothed with the general power of management incident to ownership. The applicable general rule is well expressed in *State Public Utilities Commission ex rel. Springfield v. Springfield Gas & E. Co.* (291 Ill. 209, 234, P. U. R. 19200, 640, 125 N. E. 891):

"The commission is not the financial manager of the corporation, and it is not empowered to substitute its judgment for that of the directors of the corporation; nor can it ignore items charged by the utility as operating expenses unless there is an abuse of discretion in that regard by the corporate officers."

Upon that point there was no dissent. The decision gave the State commissions much concern. It seemed to them indefensible that a holding company should be able through a subsidiary to make a contract with itself which, though appearing to the commission unreasonable, on the basis of evidence before the commission, could not be attacked without a showing of bad faith. That, however, was the ruling of the court.

The decision, I think I may say, was never acquiesced in by the State commissions. Finally, another telephone rate case came to the United States Supreme Court involving purchases of equipment by the Illinois Bell Telephone Co. from the Western Electric Co., both being subsidiaries of the American Telephone & Telegraph Co.

The company depended upon the Southwestern Bell decision to establish that any inquiry into the prices paid for equipment bought by the operating utility was an invasion of the field of management. On this point, however, the Court, through Chief Justice Hughes, ruled with the commission; and sustained its right to inquire into the cost of the equipment to the Western Electric Co., 282 United States 133, 152, 153.

Wholesale interstate utility service is not subject to State regulation. It has for a long time been held by the United States Supreme Court that a State cannot regulate the price for gas sold at wholesale by a company which transmits the gas in interstate commerce. *Public Utilities Commission of Kansas v. Landon* 249 United States 285; *Kansas Natural Gas Co. case*, 265 United States 297.

In the *Attleboro Electric Light Co. case* this principle was applied for a contract for the sale of electric energy at wholesale, 273 United States 83, 87.

(768) In that case the Rhode Island commission sought to fix the price to be paid the generating company in Rhode Island for power taken into Massachusetts and distributed there. The Court held that the transaction was interstate in character and beyond the power of the State to regulate. I will read a portion of the opinion:

In the *Pennsylvania Gas Co. case* the company transmitted natural gas by a main pipe line from the source of supply in Pennsylvania to a point of distribution in a city in New York, which it there subdivided and sold at retail to local consumers supplied from the main pipes laid through the streets of the city. In holding that the New York Public Service Commission might regulate the rate charged to these consumers, the court said that while a State may not "directly" regulate or burden interstate commerce, it may in some instances, until the subject matter is regulated by Congress, pass laws "indirectly" affecting such commerce, when needed to protect or regulate matters of local interest; that the thing which the New York commission had under taken to regulate, while part of an interstate transmission, was "local in its nature", pertaining to the furnishing of gas to local consumers, and the service rendered to them was "essentially local" being similar to that of a local plant furnishing gas to consumers in a city; and that such "local service" was not of the character which required general and uniform regulation of rates by congressional action, even if the local rates might "affect" the interstate business of the company.

In the *Kansas Natural Gas Co. case* the company, whose business was principally interstate, transported natural gas by continuous pipe lines from wells in Oklahoma and Kansas into Missouri, and there sold and delivered it to distributing companies, which then sold and delivered it to local consumers. In holding that the rate which the company charged for the gas sold to the distributing companies—those at which these companies sold to the local consumers not being involved—was not subject to regulation by the Public Utilities Commission of Missouri, the court said that, while in the absence of congressional action a State may generally enact laws of internal police, although they have an indirect effect upon interstate commerce, "the commerce clause of the Constitution, of its own force, restrains the States from importing direct burdens upon interstate commerce," and a State enactment imposing such a

"direct burden" must fall, being a direct restraint of that which in the absence of Federal regulation should be free. * * *

It is clear that the present case is controlled by the *Kansas Natural Gas Co. case*. The order of the Rhode Island Commission is not, as in the *Pennsylvania Gas Co. case*, a regulation of the rates charged to local consumers, having merely an incidental effect upon interstate commerce, but is a regulation of the rates charged by the Narragansett Co. for the interstate service to the Attleboro Co., which places a direct burden upon interstate commerce. Being the imposition of a direct burden upon interstate commerce, from which the State is restrained by the force of the commerce clause, it must necessarily fail regardless of its purpose.

That case has been accepted by everybody as establishing the distinction between wholesale and retail business and as establishing the fact that the State cannot regulate wholesale transactions, although it can regulate retail service and rates. It therefore follows that if there is to be any regulation of the wholesale part of the electric and gas business which passes over State lines it must be supplied by the Federal Government.

State commissions may pass upon the reasonableness of payments made by operating companies to affiliates: The Illinois Bell Telephone case, which I have cited, appeared to establish the principle that a State commission may examine contracts between affiliated companies and may refuse to recognize payments made to an affiliate in excess of the value of the service obtained from the affiliate. That this has been clearly established in two cases decided since the opinion in that case was rendered. I incorporate into the record citation of these cases both decided by the United States Supreme Court, with the volume and page where each case will be found. In both of these

* * * * *

APPENDIX L

Hearings Before the Committee on Interstate and Foreign Commerce House of Representatives 74th Congress, 1st Session, (1935), excerpts from Testimony of Dozier DeVane, Solicitor, Federal Power Commission

L-1

PUBLIC UTILITY HOLDING COMPANIES

HEARINGS

BEFORE

THE COMMITTEE ON

INTERSTATE AND FOREIGN COMMERCE

HOUSE OF REPRESENTATIVES

SEVENTY-FOURTH CONGRESS

FIRST SESSION

ON

H. R. 5423

TO PROVIDE FOR CONTROL IN THE PUBLIC INTEREST OF PUBLIC UTILITY HOLDING COMPANIES USING THE MAILS AND THE FACILITIES OF INTERSTATE COMMERCE, TO REGULATE THE TRANSMISSION AND SALE OF ELECTRIC ENERGY AND NATURAL GAS IN INTERSTATE AND FOREIGN COMMERCE, AND FOR OTHER PURPOSES

PART 1

FEBRUARY 19, 21, 22, 26, 28, MARCH 1, 5, 6, 7, 8, 9, 12, 13, 1935

PUBLIC-UTILITY HOLDING COMPANIES

SATURDAY, MARCH 9, 1935

House of Representatives,
Committee on Interstate And Foreign Commerce,
Washington, D.C.

(449) The committee met, pursuant to adjournment, at 10 a.m., Hon. Sam Rayburn (chairman) presiding.

STATEMENT OF DOZIER DeVANE, SOLICITOR, FEDERAL POWER COMMISSION, WASHINGTON, D.C.

The CHAIRMAN. The committee will come to order.

We have this morning Mr. DeVane, solicitor for the Federal Power Commission, who will attempt to explain the provisions of title II of the bill.

MR. DEVANE. Mr. Chairman and members of the committee, it is my understanding that at the conclusion of the hearing on yesterday your chairman announced that he would like for the hearing this morning to start with an explanation of title II of the bill; first, with an explanation of the amendments to the Federal Water Power Act—or whether he made that announcement himself or not, that is the way I prefer to present it and secondly an explanation of title II of title II.

MR. PETTENGILL. For the purpose of the record, sir, I would be glad to know who you are, and your experience.

MR. DEVANE. Well, my name is Dozier DeVane. I am solicitor for the Federal Power Commission.

MR. PETTENGILL. An attorney at law?

MR. DEVANE. An attorney at law and have been practicing since the fall of 1908.

Is there any more that you would like to know about my experience?

MR. PETTENGILL. How long have you been with the Power Commission?

MR. DEVANE. I have been with the Power Commission since the 8th of November 1933.

MR. PETTENGILL. And previous to that?

MR. DEVANE. Well, I will start back from the time I began the practice of law.

MR. PETTENGILL. Well, not in too great detail.

MR. DEVANE. I am a graduate of the Law School of Washington and Lee University. I began the practice of law in Tampa, Fla., in 1908 when I was admitted to the bar, and practiced there until the - of January 1918, when I became general counsel for the Railroad Commission of Florida.

I may say in that period I served 2 years as county attorney for the county where I resided. I was with the railroad commission 3 years,

* * * * *

(489) The purpose of that change is to avoid complications that have arisen and will continue to arise by persons proceeding with the construction of projects in waters over which Congress may have jurisdiction without a determination in advance that a license is or is not necessary. Then we strike out, near the bottom of that same page, the words "proceed with such construction" and substitute "construct, maintain, or operate such dam or other project works" making it read "Shall not construct, maintain, or operate such dam or other project works until it shall have applied for and shall have received a license under the provisions of this act."

That is to remove questions that would otherwise undoubtedly be raised in cases that will probably be brought in the future as to whether or not after a project has been constructed, the provisions of the Federal Water Power Act are applicable.

It would be argued, no doubt, in those cases that the project having been completed, the provisions of section 23 are not applicable and we hope to prevent that from arising in the future.

At this point, Mr. Mapes, I think we might clear up the difficulty that I had in answering a question that you asked me on Saturday.

You will observe that under subsection (b) of section 23, persons desiring to construct projects in waters over which Congress has jurisdiction, but which may not be looked upon as navigable waters, as such, may come to the Commission under a declaration of intention and have determined in advance of the construction whether or not a license is necessary.

That provision in section 23 is broader than the language in section 3, where the definition of navigable waters is used, the one that you were asking me about, on Saturday.

The definition of navigable waters in section 3 applies only to those waters that are in fact navigable.

Section 23 applies to waters that are not in fact navigable, but where construction may affect interstate or foreign commerce.

The provisions in section 4 with reference to the issuance of licenses uses the language "navigable waters"; for which we now propose, streams and other bodies of water over which Congress has jurisdiction."

If section 4 should be narrowly construed it can be argued that although the act requires a license under section 23, and prohibits the construction until a license has been issued by the Federal Power Commission, there is no authority in the act except in section 4 for the issuance of a license. As I told you on Saturday, it was argued in the Appalachian case that the provisions of section 23 were like the passage of a law creating a crime and providing no penalty. That is, Congress passed a law and prohibited this construction, but made no provision by which the license could be issued.

The act has been construed otherwise.

Undoubtedly, any reasonable construction of the act would lead anyone to the conclusion that the Commission could issue a license in such a case. We propose to remove any argument. I do not think we are removing doubt. All I think we do is to remove argument.

MR. MAPES. Let me be sure that I understand you. As I understand, the Commission has jurisdiction over the projects not only built upon navigable streams, but over projects that may affect (490) interstate commerce even though they are built upon waters that are not navigable or enter into navigable waters.

MR. DEVANE. That is true, sir.

MR. MAPES. Over which Congress would not have jurisdiction unless the project affected interstate commerce.

MR. DEVANE. That is right.

MR. MAPES. Yes. Has the court sustained the Commission in this respect, the jurisdiction of the Commission?

MR. DEVANE. Of nonnavigable waters?

MR. MAPES. Yes.

MR. DEVANE. You are asking about the jurisdiction of Congress over these nonnavigable waters, that affect navigation?

MR. MAPES. Yes.

MR. DEVANE. Yes; the jurisdiction of Congress over such streams was upheld in the case of the *United States v. Rio Grande Dam –gation Co.*, 174 U. S. 690. That was decided under the Rivers Harbors Act of 1899, which in effect is the same as section 23 of the act.

Also the district court, Judge Way, sustained the Commission's jurisdiction in such cases in the Appalachian case, but that particular point was not passed upon by the Court of Appeals, or the Supreme Court in that case.

MR. MAPES. My understanding of that position is that 63 out of 125 applications for permits have been made.

MR. DEVANE. Yes, sir.

MR. MAPES. And the Commission found that 63 did not come within the jurisdiction of the Commission.

MR. DEVANE. That is right. That they were going to be constructed in waters that would not affect interstate or foreign commerce in accordance with the findings made by the Commission in a particular case.

MR. MAPES. I hope you will be able to tell before you get through how large those 63 projects were.

MR. DEVANE. How large they were?

MR. MAPES. Yes.

MR. DEVANE. That may take a little time, but if you will give us time, we will be glad to furnish that information before these hearings are closed.

The only other amendment that I need to refer to is to section –. You will observe an amendment made at the end of that section. I won't bother to read it, because I ask that it be eliminated.

The Forest Service suggested that we take over the supervising permits that had been issued by it for some projects on Government lands, which is under its supervision. The amendment here is part of that proposed amendment to the act. After careful consideration of the question, the commission determined that it would notify Congress to give it that authority.

The CHAIRMAN. That is, the provision at the bottom of page 29 of the memorandum?

MR. DEVANE. Yes; and that is at the bottom of page 29.

The rest of the language was stricken out, but in some way failed to get out.

Now, with that, unless there are some questions in connection to the other amendments to the act, I will be glad to pass to title II of title II of this bill.

* * * * *

(496)MR. DEVANE. I have it here, and I would like to have it read into the record, a statement showing in each State the jurisdiction over accounting, capitalization and securities, depreciation, rates, and services.

It shows that 12 States have no jurisdiction over accounting, that 18 States have no jurisdiction over capitalization and securities, 36 States have no jurisdiction over depreciation; and that 7 States have no jurisdiction over rates and services; and you can, from that memorandum, see which of the States have jurisdiction with reference to the several subject matters mentioned.

MR. PETTENGILL. May I ask at that point, has there been any effort made to obtain uniform State legislation governing the power industry?

MR. DEVANE. No, sir.

MR. PETTENGILL. Would that not be a rather desirable way of going about some of these objectives?

MR. DEVANE. Well, the American Bar Association, which is the initiator of such legislation, has never made any progress in that direction. Each State wants to pass its own regulatory laws, and it has never, so far as I know, been considered by the American Bar Association, and it has never met with any enthusiasm or cooperation by the members of the public-utilities section of the association.

(The statement above referred to is as follows:)

State control over electric public utilities. May 16, 1934[1]

State	Accounting	Capitalization issues of Securities	Depreciation	Rates	Services
Alabama	Yes	Yes	Limited	Yes	Yes
Arizona	Yes	Yes	Yes	Yes	Yes
Arkansas	No	Yes	No	Yes	Yes
California	Yes	Yes	Yes	Yes	Yes
Colorado	Yes	No	Yes	Yes	Yes

[1] No jurisdiction over accounting in 12 States, none over capitalization and securities in 18 States, none over depreciation in 36 States, none over rates in 7 States, and none over services in 7 States.

Connecticut	Yes	No	No	Yes	Yes
Delaware	No	No: no commission.	No	No	No
District of Columbia	Yes	Yes	Yes	Yes	Yes
Florida	No	No	No	No	No
Georgia	Yes	Yes	No(?)	Yes	Yes
Idaho	Yes	No	Yes	Yes	Yes
Illinois	Yes	Yes	Yes	Yes	Yes
Indiana	Yes	Yes	Yes	Yes	Yes
Iowa	No	No	No	No	No
Kansas	Yes	Yes	Yes	Yes	Yes
Kentucky	Yes	Yes	Yes	Yes	Yes
Louisiana	No	No	No	Yes	Yes
Maine	Yes	Yes	No	Yes	Yes
Maryland	Yes	Yes	No	Yes	Yes
Massachusetts	Yes	Yes	Yes	Yes	Yes
Michigan	Yes	Yes	No	Yes	Yes
Minnesota	No	No	No	No	No
Mississippi	No	No	No	No	No
Missouri	Yes	Yes	Yes	Yes	Yes
Montana	Yes	No	No	Yes	Yes
Nebraska	No	Yes	No	Electric only	No
Nevada	Yes	No	No	Yes	Yes
New Hampshire	Yes	Yes	Yes	Yes	Yes
New Jersey	Yes	Yes	Yes	Yes	Yes
New Mexico	No	No	No	Yes	Yes
New York	Yes	Yes	Yes	Yes	Yes
North Carolina	Yes	Yes	Yes	Yes	Yes
North Dakota	Yes	Yes	No	Yes	Yes
Ohio	Yes	Yes	Yes	Yes	Yes
Oklahoma	Limited	No	No	Yes	Yes
Oregon	Yes	Yes	Yes	Yes	Yes
Pennsylvania	Yes	Yes	Yes	Yes	Yes
Rhode Island	Yes	Yes	No	Yes	Yes
South Carolina	Yes	Yes	No	Yes	Yes

(497) MR. DEVANE. I will now take up the provision of the bill. Section 201, page 103, defines the jurisdiction conferred upon the Federal Power Commission by the new title.

It states that—

The provisions of this title shall apply to the transmission and sale of electric energy in interstate commerce and to the production of the energy for such transmission and sale.

Commissioner Seavey has already pointed out that in some way the past few words of the first sentence of this section are not as we should like to have them and suggested after the word "sale", in line 22, the balance of that sentence be stricken out and that there be substituted instead the following:

shall not apply to the retail sale of electric energy in local distribution.

I shall discuss this title upon the assumption that this amendment shall be incorporated in the section.

MR. WOLVERTON. Will you repeat it again?

MR. DEVANE. "But shall not apply to" —

MR. WOLVERTON. In line 22?

MR. DEVANE. Line 22, after the word "sale" [reading]:

shall not apply to the retail sale of electric energy in local distribution.

MR. MERRITT. That means local, in any State, whether the State introduces it or otherwise?

MR. DEVANE. Yes; that is true, and I will come to that in a few moments.

MR. MARTIN. That makes section 201 (a) the same as section 301 (b).

MR. DEVANE. How is that?

MR. MARTIN. That makes section 201 (a) read the same as 301 (b).

MR. DEVANE. That is right, the same as 301 (b), with the change of electric for gas. That is on page 141 of the bill.

Now, in order to get a complete understanding of the effect of section 201 it is necessary that that section be considered in connection with section 211, 214, 217 and 309.

I will make reference to these sections as I talk about section 201. I would like to say first that insofar as rates are concerned that Section 201 is intended to give the Federal Power Commission jurisdiction over the wholesale rates only; rates over which the State (498) commissions have no jurisdiction as decided by the Supreme Court of the United States in the *Public Service Commission v. The Attleboro Steam & Electric Co.* 273 U. S. 83.

Now, that is so far as rates are concerned.

It does not extend the jurisdiction, and it is not intended to extend the jurisdiction to cases such as the *Pennsylvania Gas case* decided by the Supreme Court, where the energy was transmitted in interstate commerce over the State line and sold by the same company for local distribution. It is our opinion that under the decision of the Supreme Court in that case, the jurisdiction of this Commission might be extended to that kind of a case; but this bill does not go that far. The bill only applies to interstate rates at wholesale in interstate commerce.

* * * * *

(518) At the outset of my discussion of title II of title II, I pointed out the provisions in connection with the jurisdiction conferred by the title, called attention to the fact that insofar as rates were concerned the title conferred jurisdiction upon the Federal Power Commission over wholesale rates that were not subject to control by State Commissions under the decision of the Supreme Court in the Attleboro case. I also called attention to the fact that this bill preserves in the State commissions the power to regulate retail rates even where the power is transmitted in interstate commerce, and which might be regulated by this Commission; that we had reserved to the States the principle announced by the Supreme Court of the United

States in the Pennsylvania Gas Co. case; that insofar as facilities were concerned, that the jurisdiction conferred upon the Federal Power Commission was that the Commission should have jurisdiction over transmission facilities that were used in interstate commerce and production facilities that were connected with such transmission facilities.

The necessity for the jurisdiction insofar as facilities are concerned will be discussed in the second part of my discussion of the bill.

The first thing I was trying to do—

The CHAIRMAN. You have 50 minutes, Mr. DeVane.

MR. BULWINKLE. Will he be back tomorrow?

The CHAIRMAN. No.

MR. BULWINKLE. Because of this reason. I thought yesterday we would let him finish his statement.

The CHAIRMAN. I thought that he would finish in 50 minutes.

MR. WOLVERTON. There are a few things that I want to know before we get through.

The CHAIRMAN. Go ahead.

MR. DEVANE. If you will let me make my statement, it may be that a good many of the questions will be answered.

MR. BULWINKLE. That is what I wanted to do, in order to save time.

MR. DEVANE. I indeavored to show on yesterday, how this act would be a complement to State regulation of local rates. I call the committee's attention to section 211 page 116 of the bill, in which the Commission is given the authority to ascertain for the purpose of this title, and title III of title II, the actual legitimate prudent cost of properties of every public utility subject to its jurisdiction. Then I mentioned paragraph (b) of that section, which is merely procedural and gives the Commission access to information for the determination of such costs; and then I was right at the point of asking the committee to permit me to postpone any discussion of subsection (c) of that section at that time—

MR. BULWINKLE. You mean subsection (c)?

MR. DEVANE. Subsection (c) of that section, at this time, because that relates to the powers of this Commission in connection with the fixing of rates and what I am trying to do at this time, before I discuss those matters, is to get clearly before the committee the plan of this bill.

When I have done that, I think we can discuss these legal questions that you may ask me, with a little better understanding.

I now call your attention to the provisions contained in section 214, page 119 of the bill. Subsection (a) provides that the Commission may refer any matters originating in the administration of this act to boards made up of State commissions or State representatives.

(519) that is intended as a cooperative provision and is in practically the exact language of the Communications Act. But I also wish to call your attention to subsections (b) and (c), and particularly to subsection (c) of this section, in which we go further than Congress went with the Communications Act. This subsection makes the body of information that this Commission collects regarding this industry available for the use of State commissions in their regulatory matters, upon their request. In other words, it is a command to the Commission to do the things required under this section and when the State commissions request it, to make the information available to them. That is further cooperation in aid of State regulation of local rates than the Congress has gone either in the Interstate Commerce Act or in the Communications Act.

I next wish to call your attention to section 217, page 122. Notwithstanding the attempt so far as possible to make it clear that the bill does not usurp State authority, we added section 217, which specifically declares that nothing in this title shall be construed to impair or diminish the power of any State commission.

I also wish to call your attention to section 208 (c), on page 115, which provides that the Commission shall, upon request of any State commission, investigate and determine the cost of the

production and/or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such power.

That applies to cases that fall within the Pennsylvania Gas Co. case where the State commission is still left with the power to regulate the rate but due to the difficulties that some of these State commissions have met in their efforts to regulate such rates, because a good part of the property that was used in the production and transmission of that energy was property outside of the State, we thought it desirable to this bill to provide that the State commission could call upon this commission to make a determination of the cost of that property and to submit that information to the States. This provision is intended as a complement to State regulation.

Under section 309, page 132 of this bill, the Commission is authorized and directed to conduct investigations regarding the generation, transmission, and distribution of electric energy, however produced, throughout the United States and its possessions, whether or not otherwise subject to the jurisdiction of the Commission and submit it to Congress.

That is information which is of the character this Congress has directed the Commission to obtain in its rate survey and it is, we think, very beneficial in times of war to the Government; very beneficial to the Congress; and very beneficial to the State commissions.

Now, all of those provisions, when you analyze them, are complements to State regulation and in no way supersede State regulation.

Having given that picture—

MR. WOLVERTON. Mr. DeVane, right there, on the question of investigation: Last year, a joint resolution entitled "Authorizing necessary funds to conduct an investigation regarding rates charged for electric energy and preparing a report thereon", approved April -4, 1934, authority was given to the Federal Power Commission to investigate and compile the rates

charged for electric energy and services to resident, rural, commercial, and industrial consumers (520) throughout the United States, by private and municipal corporations and to report such rates together with an analysis thereof to Congress at the earliest practicable date.

What progress has been made in response to that resolution?

MR. DEVANE. Substantial progress has been made.

MR. WOLVERTON. Has any report been made?

MR. DEVANE. Yes, sir; that is this preliminary report to which I referred this morning.

MR. WOLVERTON. Has it been submitted to Congress?

MR. DEVANE. Yes, sir.

MR. WOLVERTON. It seems to me that the information might be very helpful in considering this bill.

MR. DEVANE. I think it would be, sir. I referred to it on yesterday.

Every Member was mailed a copy of that report.

MR. WOLVERTON. I am sorry but I do not have it.

MR. BULWINKLE. I will let you have mine if you want it.

MR. WOLVERTON. You do not think that it is of any value then.

MR. BULWINKLE. I have read it; but I will let you have mine.

MR. WOLVERTON. My mind is not made up. I will be pleased to read it for the information it contains.

MR. DEVANE. There will be in the course of the next few weeks a supplement to that report as the report states.

Now having attempted to show this committee the plan of this with reference to the regulation of rates and how it seeks to in the State commissions the power to regulate the retail rates through some Federal agency assist State commissions making available to them proper data for the determination of those rates I would like to now pass to a consideration of the integrated system I think we can take judicial notice of the fact that these competitors have now passed beyond State lines and are engaging in interstate commerce to such an extent that Federal regulation in this respect has become necessary.

I would like to call your attention to what we propose an– –tion – –

MR. HOLMES. May I ask one question before you pass on to that.

MR. DEVANE. Yes, sir.

MR. HOLMES. Of what value is this going to be to the State commissions, if you are through this bill not only trying to keep – of the transmission in interstate or foreign commerce, but you are also seeking to control the production and distribution of that energy?

MR. DEVANE. Well, that—

MR. HOLMES. Now, if you take over the production and distribution of that energy, what value is this going to be so far as the commissions are concerned, because then you have absolute power.

MR. DEVANE. I do not think that is the case. The purpose of the bill is to make energy available for local distribution that is efficient and most economical. That is what we attempt to accomplish by this bill to make an abundance of economical power available for local distribution and when that is accomplished, and the necessary information is given State commissions to enable them establish proper rates, then the problem of regulation should – so hard and we should no longer have the feeling that is abroad – that the rates of this industry are too high.

(521) MR. HOLMES. Does not section 208 give you that authority over State commissions?

MR. DEVANE. No authority over State commissions, sir.

MR. HOLMES. Where you control the production and distribution system or facilities that are engaged in interstate or foreign commerce?

MR. DEVANE. Yes; we have jurisdiction over certain facilities. That is the question I am coming to right now.

MR. HOLMES. Well, that may clear up my point. I will be glad to hear you.

MR. DEVANE. Mr. Ryan calls my attention to the fact that you used the word "distribution", and I fell right in with your words in the discussion. Let me correct that, because we do not have any jurisdiction over distribution facilities, but I will clear that up in considering the section covering that subject.

MR. HOLMES. That is my understanding that you are trying here to control not only distribution or the sale of energy through interstate and foreign commerce, but also the distribution and facilities of manufacture.

MR. DEVANE. No; we do not. I want to make that clear; we do not, no, sir.

I call your attention to sections 202 and 203.

MR. MONAGHAN. Before you go on, I want to say that I do not regard my question of yesterday as having been answered.

I am of the opinion that electric energy, when it once starts to cross State lines, the electric line being the carrier, that that energy interstate commerce.

MR. DEVANE. That is right.

MR. MONAGHAN. Interstate electrical energy.

MR. DEVANE. That is right.

MR. MONAGHAN. And that the power is vested in this Congress to regulate that interstate electric energy.

MR. DEVANE. There is no doubt about that.

MR. MONAGHAN. But, I believe—I may be wrong in assuming it—but, I believe that this amendment which you offered yesterday on page 103 of the bill would destroy the effect of this legislation as to the consuming public.

MR. DEVANE. It does not.

MR. MONAGHAN. In other words, if you regulate merely as to a wholesale dealer in electricity, then control over retail rates will only be left to weak-kneed State commissions which are controlled in so many instances by the power companies.

MR. DEVANE. This bill does not undertake to regulate the price –nd in retail distribution. I have stated to the committee—

MR. MONAGHAN (interposing). Of interstate electricity.

MR. DEVANE. Yes, sir. I have stated to the committee several times that those rates, even where the energy is transported in interstate commerce, that comes within the *Pennsylvania Gas Co. case* decision, are still left with State commissions.

Now, the *Pennsylvania Gas Co. case* was a case where the energy was produced entirely in one State and distributed entirely in another State and there the State commission attempted—it was produced in Pennsylvania and sold in Jamestown, N.Y.—and there the New York commission established those rates. The company took the position that was regulation of interstate commerce which the State commission could not do.

(522) The Supreme Court said it is true it is interstate commerce but Congress not having acted upon that particular matter, the local distribution and sale of that energy is of such a local character, the State commission could fix that rate until Congress acted and that is still left the law by this bill.

MR. MONAGHAN. That is, you are wanting to have the Supreme Court legislate that matter, in other words?

MR. DEVANE. No, sir; we are not.

MR. MONAGHAN. In other words, destroy and nullify the power of the Congress to regulate interstate electric energy.

MR. DEVANE. We are proposing something that you, as a Member of Congress, may not be willing to do; that is, we are still leaving that energy subject to State regulation.

MR. MONAGHAN. Then, the question might properly be raised that that is interstate electric energy—

MR. DEVANE. It is. It was so held in the Pennsylvania Gas Co. case.

MR. MONAGHAN. Yes. There is no question about it.

MR. DEVANE. Yes; it is.

MR. MONAGHAN. And the Supreme Court said because Congress has not seen fit to regulate, we will leave it to the State commissions.

MR. DEVANE. Congress can go much further insofar as rate regulation is concerned than we propose to go in this bill, if that is what you mean.

MR. MONAGHAN. I am interested in this bill as it affects the consumer, the rates of the people every time they turn on a vacuum cleaner, or electric light bulb, or use it for the various things, such as refrigerators, and all of the various electrical equipment that we know are used by the consuming public of today, and in seeing that they will not be charged excessive rates.

Now, I can see that this amendment would destroy the effect of the bill insofar as that particular thing is concerned, or the regulation of the rate to the consuming public.

MR. DEVANE. That is right.

MR. MONAGHAN. It would regulate utilities only as to the wholesale dealer, but it would not regulate them as to retail to the person who buys the electric energy.

MR. DEVANE. We do not, by this bill, confer any jurisdiction upon the Federal Power Commission to fix the local rates. That is correct, sir. That authority is not given by this bill. If that is the wish of Congress—

MR. MONAGHAN. This amendment specifically would deny the power to regulate retail rules, would it not?

MR. DEVANE. Yes. This commission has only the power that Congress delegates to it; this bill does not delegate that power to it; and this bill states that it is not the intention of Congress to delegate that power to the Commission; that is right. Congress in this bill makes the declaration that it does not intend by this legislation to confer that jurisdiction upon the Federal Power Commission. And Congress says further in this bill:

We are going to leave that with the State commissions, but we are going to help the State commissions accomplish the kind of regulation that the people of this county are entitled to.

(523) MR. MONAGHAN. But, the State commissions, as I see it, under a strict interpretation of interstate electric energy, would have no power to regulate that, and if not defined specifically in

this bill and properly relegated to the Commission a proper control over that interstate electric energy is virtually destroyed.

MR. DEVANE. My answer to that is that the bill as it is drawn today follows the decisions of the Supreme Court up to this time. If after this bill becomes the law, the Supreme Court should ever decide that there is any part of this industry that has not been subjected to Federal jurisdiction, and cannot be regulated by the States because of its interstate character, then I think the Congress should confer that additional power upon this Commission.

MR. MONAGHAN. In other words, you are writing the Supreme Court's decision into this bill in order to prevent that, in effect.

MR. DEVANE. Yes, sir; we are writing the Supreme Court decisions in this bill. That is correct.

MR. MONAGHAN. But, the Supreme Court said in that case that the reason it believed that it should uphold the act of the State commission of New York was because the Congress had not seen fit to act.

MR. DEVANE. That is right.

MR. MONAGHAN. And here you are saying that Congress should not see fit to act.

MR. DEVANE. That is right, we are here saying that we should not step in, that Congress will not usurp that particular power but leave it with the States.

MR. WOLVERTON. My friend's questions indicate that the amendment that you suggested yesterday was to change the meaning of the bill as it was introduced; but as I understood it was only to make clear what was your contention.

MR. DEVANE. That is correct.

MR. WOLVERTON. So, in other words, your amendment was not introduced to change the policy which you thought the bill had completely set forth, but merely to make the policy clear.

MR. DEVANE. To make the policy definite and so that there would be no question about it. There have been a number of questions asked which indicate that some members of the

committee think the language in this bill goes entirely too far, and we want to make it clear as to the purpose of this bill.

MR. WOLVERTON. Maybe if that amendment has the effect Mr. Monaghan thinks it has, it may get Presidential approval as not being too drastic.

MR. DEVANE. May I pass on?

The CHAIRMAN. Mr. Kenney desires to ask a question.

MR. KENNEY. Can you give us your definition of "regulation"? I am interested to know whether it includes elimination.

MR. DEVANE. No, sir; my definition of regulation would not include elimination.

MR. KENNEY. And in this title II, is there any power given the Commission to eliminate any existing conditions?

MR. DEVANE. Conditions?

MR. KENNEY. Yes

MR. DEVANE. Well there is power to eliminate existing conditions if I understand your question—

(524) MR. KENNEY. Well, is the power given to eliminate any present lines transmitting electrical energy?

MR. DEVANE. Well, no; the power is not given to eliminate any present lines. That may be accomplished in other ways, but the power to eliminate present lines is not given.

MR. KENNEY. How would you accomplish that?

MR. DEVANE. It may be accomplished this way if present facilities are entirely inadequate to properly serve the public convenience and necessity, additional facility may be required which will in fact supersede the present facility, and in that way, the present facility would be eliminated.

MR. KENNEY. Would that drive out of business some existing companies that might be interested in that line?

MR. DEVANE. No, sir; all questions of the kind you are asking should presuppose that anything the Commission does is in the public interest and is right and if it is in the public interest and is right, it should be done—that is, insofar as facilities are concerned—the construction of new facilities, elimination of

present facilities, or the extension of facilities. It must always be assumed that the thing that the Commission orders done is in the public interest or it has no right to order it done. If it is not in the public interest then the company against whom the order is issued has its resort to the court to prevent it. The approach to the power given the Commission under this bill with reference to the extension of facilities or with reference to any other matter must be predicated upon the assumption that all such powers will be exercised in the public interest.

MR. KENNEY. And, we have to assume that the Commission is always right in that regard?

MR. DEVANE. No, sir; you do not have to assume that.

MR. KENNEY. I so inferred from what you said.

MR. DEVANE. You mean up to the point where the Commission has passed upon it?

MR. KENNEY. Yes. And for review by the courts of the decision of the Commission, would certiorari be required in order to bring up all of the facts to have the court pass on them?

MR. DEVANE. No, sir; the act provides for a direct appeal to the circuit courts of appeal in the several circuits in the United States, in the circuit where the controversy arises.

MR. KENNEY. And the appeal would permit a review of factual questions by the court?

MR. DEVANE. It goes up on the record that was made before the Commission, with the proviso that if the utility needs some additional evidence that it could not present at the hearing before the Commission, it may petition the court and present it.

The CHAIRMAN. It is the usual procedure, is it not?

MR. DEVANE. Yes, sir.

Mr. CROSSER. Mr. Chairman—

The CHAIRMAN. Mr. Crosser.

MR. CROSSER. Mr. DeVane, just before passing on, may I ask just one question, as to whether it is your's or the Commission's idea in limiting the power to regulate merely to wholesale disposition of power rather than wholesale and retail, so as to

avoid controversies or do you think this is sound political economy?

(525) MR. DEVANE. I think it is sound economy. I think this bill offers, if I may be permitted to say so with some modesty, that this bill offers a plan of regulation that fits into our system of government as well as, and I would like to say, better than, either the Interstate Commerce Act or the Communications Act, in that it establishes more cooperation between the States and the National Government. It permits them to function in unison. The Communications Act went a long way in that regard, but this bill goes even further.

MR. MONAGHAN. Mr. DeVane, you say in effect that you are leaving the regulation of interstate electric energy to the State commissions. You are in effect saying they can do a thing, or you are going to help them do a thing, which patently they cannot do.

MR. DEVANE. Well, my answer to that question is this, we are lending the aid of the Federal Government to them to see if this kind of regulation cannot be accomplished in this way.

Now, if this is a failure, or if this industry is able to defeat proper and adequate regulation under this law, and the States are not able to function, then I think Congress must take the second step; but let us do not take it until we have given this matter a trial.

MR. MONAGHAN. If I can make myself clear on that point—

MR. MERRITT. You do not want to abolish the States unless we have to.

MR. MONAGHAN (continuing). I am trying to argue to this situation: Here is an electric energy that emanates from the State of Connecticut, we will say, or Montana. Take whatever State you wish. And, it is distributed in the State, we will say, taking Montana as the example, it is distributed in the state of Wyoming. That is clearly interstate electric energy. As such, the Congress and the Congress alone has the power to regulate it; but the effect of what you are saying here is that the States have the power and we will just cooperate with the States.

MR. DEVANE. Yes

MR. MONAGHAN. And, I cannot see but that is just passing the buck, and not standing right up under the guns here and saying Congress will do the thing which it should do, regulate those rates in the interest of the public, and I think this amendment has that effect.

MR. DEVANE. If you do not make the purpose clear you would reach out and control that energy.

MR. LEA. Mr. Chairman— . . . .

The CHAIRMAN. Mr. Lea.

MR. LEA. In section 217 of this bill it is provided that:

Nothing in this bill shall be construed to impair or diminish the powers of the State commission.

Now, from what you have said I take it that you construe those powers of the State commissions as including the powers they now exercise because the Federal Government is not occupying the field; is that true?

MR. DEVANE. Yes; that is true. Let me make this clear to you, if this bill provided for the regulation of all energy in interstate commerce but nevertheless contained that provision in it, I do not think that provision in and of itself would override the other provisions and leave the power in State commissions that they now have under (526) the Pennsylvania Gas Co. decision; if I may make that point to you.

Mr. LEA. Well, I take it that the power of the State commissions if we permit this language to remain, would include not only the power that the State commissions are now exercising, but the powers that they could exercise at the present time in the absence of Federal control.

MR. DEVANE. If this act attempted to exercise all of the power that Congress has then that provision would be construed in that light and it would mean that Congress had taken from the States all the power they now have except that reserved to them under the Constitution.

On the other hand, if you come along and say as you do in this bill that there is a certain class of this business that you do

have jurisdiction over, but assert that you are not going to take jurisdiction of it, but are going to leave it with the States the effect is to leave that energy subject to State regulation even though it is energy over which you might assert jurisdiction.

MR. LEA. Does not that delegate to the States a function that is really a Federal function?

MR. DEVANE. Yes, sir.

MR. LEA. Is there any other instance in which the Federal Government has provided for regulation in which it has adopted this language as is contained in section 217 preventing the impairment of diminishing of a State power?

MR. DEVANE. The language of section 217 is the exact language of the Communications Act, section 213 (h).

MR. LEA. There is no regulatory measure adopted prior to that time that contains that language?

MR. DEVANE. I do not recall any, Mr. Lea; no, sir.

MR. LEA. Well, in the provision that you cited a while ago, giving the Power Commission authority to make the investigation as to costs and so forth, and authorizing them to keep the information current, would not that require constant attention to that job and virtually make the Federal Government subordinate to the State commissions, leaving the Federal Commission at the beck and call of the State commissions to perform that constant valuation service?

MR. DEVANE. It is not a valuation service, Mr. Lea. The – under that provision is simply this: I think it is a fact about which we may take judicial notice, that we do not have in this country information as to the actual cost of the property that is devoted to this service. We have book records, but we do not have costs.

Under the provisions of this bill the Commission would undertake to ascertain how much money there is invested in the interstate property of these utilities, how much it cost to construct the property. Having ascertained that, then the accumulations of your additions annually each year thereafter is a very simple matter. All that information will be made available

to the State commissions. They will know this year, the next year, and the next, what this property actually cost.

MR. LEA. Would that be with the idea of affording the State commissions ample information upon which to base rates?

MR. DEVANE. Yes, sir.

MR. LEA. Would not that be similar to the valuation we authorize with regard to the railroads which required 8 or 10 years and then was not complete?

(527) MR. DEVANE. No, sir. The difficulty that the Interstate Commerce Commission ran into under that act was in determining the reproduction cost new, and the reproduction cost new, less depreciation. That was because they had to make inventories of the property, and had to make appraisals. The determination of a historical cost is nothing like the task of determining the reproduction cost new less depreciation, provided you have records that are any good at all.

Now, if these companies have no records, if they can show that they have no records that are any good at all, then it will be a substantial job, but even then nothing like the job of the Interstate Commerce Commission.

MR. LEA. It would require the constant ascertainment of values, would it not?

MR. DEVANE. No, sir. And, so far as the future is concerned, the determination of cost will be a simple matter because it will be set up on their books under accounting regulations prescribed by the Commission which they must follow.

MR. LEA. Is there anything in this bill that would provide for the joint determination of values or rates, by the Federal and the State governments?

MR. DEVANE. Yes, sir; in 214, the cooperative section.

MR. MARTIN. May I ask a question?

The CHAIRMAN. Mr. Martin.

Mr. MARTIN. Does not the situation in the power field call for the exercise by Congress in this legislation of all of the power that it has to regulate under the Constitution and under the commerce clause?

MR. DEVANE. Speaking as an individual, and expressing an individual opinion in answer to that question, I will say that it is my opinion that this bill will accomplish everything that Congress wishes in connection with the regulation of this industry.

MR. MARTIN. Assuming that your answer had been in the affirmative, I propose then to follow it by the further question as to whether section 217 could not be dropped from the bill and leave it to the courts to determine whether the Federal Power Commission in any given case exceeded its authority and invaded the constitutional right of the State?

MR. DEVANE. Yes; the legislation could be drawn along that line.

MR. MARTIN. The legislation could be drawn with the express policy of taking into the control of the Federal Government all the power that it has for the regulation of this industry without putting that expression in the bill contained in 217; it could be just dropped out.

MR. DEVANE. Section 217 could be dropped out, yes, sir; but I would like to see section 217 preserved as a matter of congressional policy.

MR. MARTIN. It just seems to me that in 217 the Commission is standing up so straight that it is leaning backward.

MR. DEVANE. I do not so interpret it.

Mr. PETTENGILL. Well, Mr. DeVane, you have stated that in the drafting of this title II, you conferred with the different State commissions; did you not?

MR. DEVANE. Mr. Seavey stated that.

MR. PETTENGILL. That is the fact; is it not?

(528) MR. DEVANE. Yes, sir: that is the fact.

MR. PETTENGILL. Well, was section 217 put in in order to obtain their consent to the bill?

MR. DEVANE. No, sir.

MR. PETTENGILL. It was done entirely voluntarily on your part?

MR. DEVANE. Yes, sir.

MR. BULWINKLE. How many State commissions have complained to the Federal Power Commission of their lack of authority to handle this power question?

MR. DEVANE. None that I know of. There is no reason why they should.

MR. BULWINKLE. Not a one?

MR. DEVANE. No, sir.

MR. BULWINKLE. How many consumers, if any, have applied to the Federal Power Commission, or complained to the Federal Power Commission on account of the wholesale rates in interstate commerce being too high?

MR. DEVANE. The consumers.

MR. BULWINKLE. Yes.

MR. DEVANE. Now, you mean the wholesale consumers.

MR. BULWINKLE. The wholesale consumers.

MR. DEVANE. I cannot answer that question.

MR. BULWINKLE. Have there been any?

MR. DEVANE. I cannot answer that question. We have had thousands of complaints. As to how many of them are wholesale or retail, I do not know.

MR. BULWINKLE. As to how many are wholesale or retail, you do not know?

MR. DEVANE. No.

MR. BULWINKLE. But, there has not been a single State commission that has made any complaint to you at any time or any statement to you at any time asking for Federal regulation prior to the enactment or rather the drafting of this bill?

MR. DEVANE. Now than, as I understand you, if I understand the character of your question, you mean—

MR. BULWINKLE. How many have complained?

MR. DEVANE. The State commissions, the State commissioners that considered this bill endorsed it and—

MR. BULWINKLE (interposing). But, I understood from Mr. Seavey when he was on the stand that title II was not in the bill when they endorsed it.

MR. DEVANE. Oh, it was; title II of title II.

MR. BULWINKLE. Was that all of the State commissions?

MR. DEVANE. It was taken up through their national association here in Washington.

MR. BULWINKLE. Who represents them here?

MR. DEVANE. The executive committee and the legislative committee of the national association. Mr. Benton, who is their Washington representative, will appear here as a witness and he can furnish the names of the men that are on the executive committee and the names of the men that are on the legislative committee; but it was taken up and the committees were called in session.

I believe Mr. Seavey offered the resolution of the executive committee with reference to this bill.

(529) MR. BULWINKLE. But, prior to that time—I want to get it straight—prior to that time, not a single State commission had complained to the Federal Power Commission about their lack of authority to handle this situation.

MR. DEVANE. Well, that is little too broad an order for me, because I do not know whether they had or not. I could not answer that question.

MR. BULWINKLE. You have not heard of any?

MR. DEVANE. I have not heard of any.

The Chairman of the Commission, Mr. McNinch, calls my attention to the fact that you will find in many of the annual reports of the State commissions, statements to the effect that Federal legislation should be enacted to control holding companies and interstate wholesale contracts.

MR. BULWINKLE. You do not know which States though; where that is?

MR. DEVANE. No, sir; I have not examined those reports.

The CHAIRMAN. They all know that they did not have any power to do it.

MR. DEVANE. Yes, sir.

MR. BULWINKLE. That might be some of those 12 that do not have any State powers to do it.

The CHAIRMAN. I think their resolution stated in endorsing this bill that they say that they think it is necessary in order to bring about effective State regulation that there be Federal regulation over these matters that they cannot reach by State authority.

MR. BULWINKLE. The reason I asked, Mr. DeVane, I notice in the papers that the Georgia Utilities Commission announced that they were coming to Washington to fight this bill.

The CHAIRMAN. Yes; on the theory that it was taking away from them some of their jurisdiction; not on any other theory, because I think I have talked with practically every Congressman from Georgia or every one of them has talked to me about it, and upon being assured that this bill did not take jurisdiction away from their commission, they seemed to be perfectly satisfied.

MR. DEVANE. Due to the error that occurred in subsection 201 (a) there was plenty of justification for the effort that has been made to convince State commissions that it was the purpose of this bill to take power away from them, and that representation could be fairly made to them, and since the bill has been introduced, I have heard it stated that was the concealed purpose of this commission, and probably might be the intention of Congress; but I want to make it perfectly clear here that it is not the purpose or desire of the Commission, and we trust that when the legislation comes out of Congress that it will leave to the State commissions as much authority as can be left with them.

The CHAIRMAN. And you want the act to be perfectly clear on that point.

MR. DEVANE. I want the act to be perfectly clear on that point.

MR. BULWINKLE. The reason I asked you was I notice in my mail from 150 to 200 letters a day and there has never been one from the State commission asking me to support it.

MR. COLE. Mr. Chairman, may I ask a question?

(530) The CHAIRMAN. Mr. Cole.

MR. COLE. Following the line of questions for the last 3 or 4 minutes, regardless of whether the State commissions have complained or not, it is a fact that it is terrifically expensive and burdensome on the State commissions to attempt to determine whether the cost of power coming into the State through interstate commerce for local distributing companies is fair or not.

MR. DEVANE. Yes.

MR. COLE. All I understand this legislation to do is to establish fair, reasonable and just costs.

If the power at the State line and from that point on through the distributing plant of the local distributing company, to the consumers is under regulations of the State law.

MR. DEVANE. Yes, with one exception, Mr. Cole, we would include in our costs, in our determination of what was a reasonable cost of that power, the cost of transmission to the point of local distribution.

MR. COLE. Oh, yes, I understand that.

MR. DEVANE. Beyond the State line to the point of the local distribution.

MR. COLE. And to determine that now through the State agencies, State commissions, is an almost impossible task, is it not?

MR. DEVANE. Oh, I think so. I think it would be just like trying to pull a freight car with a team of mules. That is a fair illustration of the difficulty as a State matter.

MR. BULWINKLE. What additional cost will it be, and I am just asking for information, assuming that this act is passed, title II is passed, to the Federal Power Commission for the personnel and all other expenditures necessary for the carrying out of these various investigations, and in enforcing the act?

MR. DEVANE. May I first make this statement: You understand, of course, the administration of the Federal Power Commission throughout its existence has been without any cost to the Government. It is maintained through charges that are imposed upon the licensees.

MR. BULWINKLE. I realize that fact.

MR. DEVANE. So far as I know, no estimate has been made of what it would cost the Government to administer the provisions of this bill, and I would say that no real estimate could be made until Congress passes the law and we know what functions are going to be administered. At that time a proper estimate can be made.

The CHAIRMAN. We will go on this afternoon. There is general debate in the House. So, we will go on this afternoon at 2 o'clock.

MR. DEVANE. We will meet here at 2 o'clock?

The CHAIRMAN. Yes.

(Thereupon, at 11:40 a.m., the committee recessed until 2 p.m. of the same day.)

AFTERNOON SESSION

(The committee reconvened, pursuant to the taking of a recess, at 2 p.m., Hon. Sam Rayburn (chairman) presiding.)

The CHAIRMAN. The committee will come to order.

All right, Mr. DeVane, you may proceed.

* * * * *

(548) jurisdiction over rates is concerned, there is absolutely no encroachment upon State authority. It is my position, insofar as 204 is concerned, there is no encroachment upon State authority. The bill, in section 203 states—

MR. BULWINKLE. Let me ask you right there: Let us suppose that we have a power company in North Carolina, Virginia, or Maryland—I do not care which—and the extension that they are going to make is purely intrastate: while they do a minor amount of interstate business, this extension is purely intrastate.

Now, they have to get a certificate of convenience and necessity from the Commission—from your Commission—to do that?

MR. DEVANE. No, sir.

MR. BULWINKLE. Well, that is an extension.

MR. DEVANE. Yes, sir: that is true. That is an extension, and that illustrates the point that I attempted earnestly to make to you yesterday. In considering the word "extension," or considering any other word in this bill, you must take into consideration the authority that is conferred under section 201.

The bill gives the Commission jurisdiction over the transmission facilities that are used in interstate commerce and the production facilities that are used in connection with those transmission facilities.

The bill does not give the Commission any jurisdiction whatever over facilities used in local distribution or the transmission facilities that are used in connection with such local distribution, unless they are also a part of the facilities that are used in interstate commerce.

MR. BULWINKLE. Then it is your opinion and your construction that if owners of this power company were to build an additional transmission line going into another State, then they would be under your jurisdiction?

MR. DEVANE. That is correct. If it is a transmission line going into another State, it must convey the energy that goes into interstate commerce. Do I make that clear to you?

MR. BULWINKLE. Do you not think that we had better amend that just a little bit, because we may have a judge that has no clearer idea of it than I have.

MR. DEVANE. I hold no brief for the words that are used to accomplish the purposes sought by the bill. I have no doubt but what you will find that there are other words that can express the same intention in language that is more satisfactory to you.

MR. BULWINKLE. Well, let me state this: My understanding of the purpose is that so far as the Federal Power Commission is concerned, I do not mean that they are asking it, but all that is asked for it is that just the power sold in interstate business, wholesale, shall be under the regulation of the Federal Power Commission; is that it?

MR. DEVANE. No, sir; you have changed your question on me again.

MR. BULWINKLE. All right, then let us try it again.

MR. DEVANE. All right.

MR. BULWINKLE. The Federal Power Commission—it is asked that the power be given to the Federal Power Commission to control all companies who are selling power in interstate, the power which is sold in interstate; give them the power to control it; is that right?

MR. DEVANE. No, sir; that is not right.

MR. BULWINKLE. Then, what is it that they are asking?

(549) MR. DEVANE. Well, I should not say it, but you discouraged me. After so many efforts to make it clear I feel that probably someone else could do it better than I can; but let me state it again.

MR. BULWINKLE. All right.

MR. DEVANE. Insofar as rates are concerned–

MR. BULWINKLE. Wait a minute. Maybe we can get what is the main objective point to title II.

MR. DEVANE. Yes; Federal and State cooperation and interconnections are the main advantages, throughout this bill.

MR. BULWINKLE. I am not talking about advantages.

What are the great objectives sought by the passage of title II of this bill?

MR. DEVANE. Two objectives are sought by the passage of this bill.

MR. BULWINKLE. Let us get those.

MR. DEVANE. One objective is complement to State regulation of rates. The second objective is regional coordination and the bringing of these properties together in systems in these regions. Those are the two main objectives of this bill.

MR. BULWINKLE. Well, then, the other thing is not considered at all—the wholesale—the right of the Federal Power Commission to regulate the wholesale price of the transmission?

MR. DEVANE. That is a part of the first objective of the bill.

The first objective of the bill is a complement to State regulation of rates, and as a part of that complement the bill provides that the Federal Power Commission may regulate the rates that no State commission can regulate. The bill simply fills this gap and that is all.

MR. BULWINKLE. And that is all that you are asking?

MR. DEVANE. That is all, insofar as the rates are concerned.

MR. BULWINKLE. All right.

MR. DEVANE. Now, when you are talking about rates, that is all; we simply fill the gap. I want that clearly understood, that that is all insofar as rates are concerned.

The second objection is the creation of regional integrated systems so as to secure the best service to the public.

MR. BULWINKLE. Well, then, the question comes to my mind, has the public not been served?

MR. DEVANE. Oh, the public has been served, but do you mean, has it been served to the best advantage?

MR. BULWINKLE. To the best advantage.

MR. DEVANE. No.

MR. BULWINKLE. In what respect; have their rates been too high?

MR. DEVANE. I think so. I think you have a fairly good answer to that in what has happened in the last 18 months. I think there has been a reduction in rates in the last 18 months amounting to an annual reduction of between 35 and 40 million dollars. To a very large degree these reductions have been voluntary on the part of the industry. I think that is a fairly good answer to your question.

MR. PETTENGILL. Mr. DeVane, I would like to ask your construction of the word "operate" in line 4, page 107.

Now, that reads:

No public utility shall undertake the construction of extension of any facilities subject to the jurisdiction of the Commission or acquire or operate any such facilities.—

Without getting a certificate of public convenience.

(550) Would that apply to facilities already existing?

MR. DEVANE. Will it apply to existing facilities?

MR. PETTENGILL. Yes; the word "operate."

MR. DEVANE. Your reference to the word "operate" goes along with the word "acquire". That is, it relates to facilities not previously owned or controlled.

MR. PETTENGILL. Well, it is not your intention to require a certificate of public convenience from existing companies to operate their existing facilities?

MR. DEVANE. No; not at all; not at all, sir. That wording is not intended to require that, and if there is any need for clarification of that, I ask that it be done, because it only applies to those facilities that might be acquired.

MR. COOPER. Mr. DeVane, may I ask you a question?

MR. DEVANE. Yes, sir.

MR. COOPER. I believe you stated a moment ago that this bill gives to the Federal Power Commission power to regulate electric energy transmitted in interstate commerce for wholesale purposes, and the production facilities?

MR. DEVANE. And the transmission facilities used in transmitting the energy.

MR. COOPER. You said production.

MR. DEVANE. Production and transmission; yes, sir.

MR. COOPER. All right now. Supposing here was an industry, 10 percent of whose business was interstate, and 90 percent was intrastate; the 10 percent interstate still gives you the power to regulate it, notwithstanding that 90 percent is intrastate, you can regulate the industry?

MR. DEVANE. It gives the Commission control over interstate transmission facilities.

MR. COOPER. And you said production.

MR. DEVANE. Coming into that, it gives the Commission jurisdiction over production facilities connected with the interstate transmission facilities.

In that respect, may I say Mr. Cooper, that it is in entire accord with every other piece of regulatory legislation Congress ever passed.

MR. COOPER. Let us understand this right now; not withstanding 90 percent of the business is intrastate and 10 percent is interstate, this bill gives you the power to regulate the entire production of the industry?

MR. DEVANE. Yes, sir.

Less than 5 percent of the telephone industry is interstate.

MR. WOLVERTON. Mr. DeVane, you spoke of the use of the word "operate" as probably being ambiguous.

I want to say it has been my experience on this committee with any bill drawn by Mr. Cohen, and Mr. Cochran, that there is nothing ambiguous in it. It is always fraught with meaning, and I cannot discount the power that seems to exist as the result of the use of language by saying it is ambiguous. I have found by experience that if they have drawn a bill that they are so careful and are so choice in the language that they use that they could give a reason for that particular wording, and it is always filled with meaning.

MR. DEVANE. Of course, I have no answer to that.

(551) MR. WOLVERTON. It might be assuring to this committee to be told that some of the words are ambiguous, but from the experience I have had in the past that would not assure me, for I have a feeling that word is there for some purpose.

Now, if you had drawn the bill and you would acknowledge that you had used ambiguous language, I would have the utmost confidence in leaving it up to you to correct that particular language; but when you suggest that their language is ambiguous, I am afraid that you have not had the experience with them that we have had.

MR. DEVANE. Do I understand from that statement, that it is your impression they drew title II of title II?

MR. WOLVERTON. We had a witness here before us who said they did.

MR. DEVANE. No, sir.

The CHAIRMAN. How is that?

MR. WOLVERTON. A witness who said they did.

The CHAIRMAN. Did what?

MR. WOLVERTON. Drew this title.

The CHAIRMAN. What witness said that?

MR. DEVANE. No not title II of title II.

MR. WOLVERTON. His statement was that the same language that appears in title II appears in title I.

MR. DEVANE. I understood that testimony related to title I only.

MR. WOLVERTON. It has already been pointed out to us that the same words are in title I and title II.

MR. DEVANE. That was in connection with sections 15 and 16.

MR. WOLVERTON. Whether those who drew title II adopted the language Mr. Cohen and Mr. Cochran used in title I or whether they adopted the language you folks used in title II, I do not know, but the fact is that the same language exists in both.

MR. DEVANE. I do not contend that anyone who had anything to do with the preparation of title II of this bill is any more qualified, or as much qualified, as Mr. Cohen or Mr. Cochran, to draft legislation. It is my understanding that they are men of great ability and are very highly regarded in that respect, and I wish I had the ability that they have. I would be very proud of it. But, I do want to say in connection with any of the statements that I have made with reference to any language used in title II of title II, that what I have said to this committee as to the purpose of this legislation, and as to the desire of the Federal Power Commission, presents the purpose and the desire of the Commission and that there is no desire whatever to obtain results through this legislation that I have not stated.

We are not using words that are ambiguous with the intention or in the hope of getting a different result when the legislation is passed. We are perfectly sincere in our efforts to accomplish

a certain purpose, and we have used language that we think accomplishes that purpose.

MR. WOLVERTON. There is no thought in what I have said of conveying the impression that I do not consider that you are perfectly honest and sincere certainly in the views that you have expressed, nor is there any intention upon my part in any way to speak detrimentally of the ability of those two gentlemen, for I have even higher respect for their ability than you have expressed that you

* * * * *

APPENDIX M

Hearings Before a Subcommittee of the Committee on Interstate and Foreign Commerce House of Representatives 80th Congress, 1st Session, (1947), excerpts from Testimony of Howard E. Wahrenbrock, Assistant General Counsel, Federal Power Commission

M-1

FEDERAL POWER ACT

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE COMMITTEE ON

INTERSTATE AND FOREIGN COMMERCE

HOUSE OF REPRESENTATIVES

EIGHTIETH CONGRESS

FIRST SESSION

ON

H.R. 2972

A BILL TO AMEND SECTION 201

OF THE FEDERAL POWER ACT

AND

H.R. 2973

A BILL TO AMEND

THE FEDERAL POWER ACT

JUNE 23, 24, 26, JULY 2, 10 AND 11, 1947

Printed for the use of the
Committee on Interstate and Foreign Commerce

(505)STATEMENT OF HOWARD E. WAHRENBROCK, ASSISTANT GENERAL COUNSEL, FEDERAL POWER COMMISSION, WASHINGTON, D.C.

Mr. HALL. Mr. Wahrenbrock, will you state your full name and the office which you hold?

Mr. WAHRENBROCK. My name is Howard E. Wahrenbrock. I am an assistant general counsel of the Federal Power Commission.

As has been indicated, I shall discuss the legal and jurisdictional phases of the Commission's views with respect to H. R. 2972—the nature and effect of the bill on the scope of regulation of interstate electric utilities under part 14 of the Federal Power Act—and explain the reasons which impelled the Commission to say in its report that H. R. 2972 must be viewed as a virtual repeal of that regulation.

Superficially, H. R. 2972 may seem to be just a series of provisos or exemptions of a few facilities, persons, and transactions from the provisions of section 201, in part II, of the act. But that section is one which defines the facilities, persons, and transactions which are brought within the Federal regulation provided by most of the other sections of part II of the act and the related provisions of part III. The effect of the exemptions is to generally withdraw from the application of the act the bulk of the facilities, persons, and transactions now regulated. Their importance can be fully appreciated only by understanding what Congress sought to accomplish by the Federal Power Act as it now stands. This is important whether those purposes are now to be adhered to, or are to be changed by Congress, for only by consistently following clearly understood purposes can the provisions relating to jurisdiction be so amended as to remain workable and be truly indicative of the intent of Congress.

PURPOSES OF PART II OF FEDERAL POWER ACT

The history of part II and the related provisions of part III of the Federal Power Act discloses that they had two principal purposes. (506) One was to regulate interstate wholesale rates and service of electric utilities which the Supreme Court under the commerce clause had held to be beyond the reach of the constitutional power of the States. The other was to strengthen and supplement State action which had been ineffective in correcting and preventing the unsound corporate and financial practices disclosed by the Federal Trade Commission's comprehensive investigation of the utility industry. A brief explanation of each of these purposes will make clear that the exemptions proposed in H. R. 2972 do not merely remove a few fringe companies from the coverage of the Federal Power Act, but substantially defeat the purposes for which it was enacted by exempting a large and important part of the industry.

1. *Regulation of interstate wholesale rates and service*

Supreme Court decisions under the commerce clause over a period of more than 15 years preceding the Federal Power Act had demonstrated that the States were constitutionally powerless to regulate the transmission or sale at wholesale in interstate commerce of electric energy or gas (*Public Utilities Commission v. Landon,* 249, U.S. 236 (1919); *Missouri v. Kansas Natural Gas Co.,* 265 U.S. 298 (1924); *Public Utilities Commission v. Attleboro Steam & Electric Co.,* 273 U. S. 83 (1927): *State Corporation Commission v. Wichita Gas Co.,* 290 U. S. 561 (1934)).

In *Missouri v. Kansas Natural Gas Co.,* the company produced and purchased gas, in Oklahoma and Kansas, and piped it into Kansas and Missouri, selling it to local distributing companies situated in the latter States. The company contended that the State commissions could not, as they had attempted,

constitutionally regulate the rates of the wholesale sales to the local distributing companies. As foreshadowed in the *Landon case, supra,* this contention was upheld. The Court made it clear that even in the absence of any action by Congress, the commerce clause, of its own force, restrains the States from assuming jurisdiction over wholesale sales in interstate commerce.

The Attleboro case appeal the — Court holding that it was beyond the power of the individual States to regulate the transmission and sale of electricity generated in one State and sold to an out-of-State purchasing company for consumption in another State. The Court made it clear that the particular point at which title passed was immaterial. Indeed, although the sale there involved took place at the State boundary, the Court relied upon a case which had held that sales in interstate commerce made in the State of origin were beyond the power of the several States to regulate, citing *Shafer v. Farmers Grain Co.* (268 U. S. 189), and upon *Missouri v. Kansas Natural Gas Co.(supra),* where the sales were made in the State to which the gas had been transported and in which the sales had taken place, so that the Court's reliance on that case emphasizes that it is inmaterial where the sale takes place.

These cases make it clear that at the time of the passage of the Federal Power Act of 1935, the individual States lacked the constitutional power to regulate the interstate transmission, and the sale at wholesale in interstate commerce of electric energy generated in one State and transmitted for consumption in another, whether the sale occurred in the State of origin, at the State line, or in the State of destination.

(507) They illustrate the wide scope of the "gap" in regulation which existed at that time. Transportation, sale, and delivery to the distributor as an unbroken chain, fundamentally interstate is beyond the regulatory powers of the States. This is the law

today, some of these cases having been cited with approval by the Supreme Court in the present term.

However, the decisions of the Supreme Court had also pretty clearly indicated the boundaries of the area in which the States were powerless, by upholding the authority of the States to regulate rates and service in local distribution of gas and electric energy although moving in a continuous, uninterrupted interstate flow to the consumer *(Pennsylvania Gas Co. v. Public Service Commission,* 252 U. S. 23; Cf. *South Carolina Power Co. v. South Carolina Tax Commission,* 52 F. (2d) 515 affirmed *per curiam,* 286 U. S. 525). Related tax cases indicated that generation of energy was within State competence, even though the energy was transmitted in interstate commerce after leaving the generator *(Utah Power & Light Company v. Pfost,* 286 U. S. 165). This was also true of interstate transmission for the transmitter's own consumption *(The Pipe Line Cases,* 234 U. S. 548).

Congress sought to plug the constitutional gap in the powers of the States by the provisions of the Federal Power Act relating to the regulation of rates and service in interstate transmission and sale at wholesale. In particular these are section 202 (b), 205, 206(a), and 207. The definitions in that act of the Commission's jurisdiction over rates and service were drawn with care to assure that the statutory plug should exactly fit the constitutional gap. The public utilities regulated by the act were defined as those persons owning or operating facilities for transmission or sale at wholesale of electric energy in interstate commerce (sec. 201). To prevent encroachment upon the powers of the States, express limitations were spelled out in section 201 (b) against any Federal assertion of jurisdiction over facilities for generation, facilities used in local distribution, facilities used only for intrastate transmission and facilities for transmission of electric energy consumed wholly by the transmitter. These provisions effectuate the declaration of policy in section 201 (a),

"such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States," as Mr. Justice Jackson pointed out in *Connecticut Light & Power Co. v. Federal Power Commission* (324 U. S. 515, at p. 527).

The enactment of Federal legislation for this purpose was not opposed, and moreover was actually sought and recommended by State regulatory agencies and their representatives. And I may point out that the former general solicitor of the National Association of Railroads and Utilities Commissioners has recently written:

This power of rate regulation, in practice thus far, has resulted in no encroachment upon the rate-making power of State regulatory agencies (Benton, John E., *Jurisdiction of the Federal Power Commission and State Agencies,* 14 Geo. Washington L. R. 53, 65-66).

2. Correction and prevention of corporate and financial abuses

At the time the State commissions were seeking Federal legislation to fill the constitutional gap in their regulation of rates and service, Congress also had before it the shocking indictment presented by the Federal Trade Commission's disclosure of the financial and corporate (508) abuses which had become prevalent in the gas and electric utility industries in spite of long attempts by the State, to regulate those industries. The electric utility industry had been subject to public regulation almost from its inception a little before 1890. Electric utilities had to have the use of public streets and highways to serve their customers. The use which could be made of streets and highways for electric service facilities naturally was limited. Practical and esthetic considerations as well as obvious considerations of economy limited the number of companies which might be permitted to use them in competing to serve customers in the same area. The protected market and practical

monopoly thus assured to the companies obtaining franchises carried obligations of public service like those of common carriers, to serve all customers seeking service, and to do so at reasonable rates sometimes prescribed by franchise or action of public authority. Other special privileges were conferred on the companies, including the sovereign power of eminent domain.

At first this public regulation was usually by the local municipality, largely through the terms of the franchises, but this was supplemented at an early date and followed by State regulation through utility commissions. The powers of such commissions were broadened from time to time and covered security issues, transactions in utility properties, and accounting, as well as rates and service.

The first Federal regulation of electric companies, provided by the Federal Water Power Act of 1920, was merely an incident to the licensing of hydroelectric projects on public lands or involving navigable waters of the United States. Initially it affected only a comparatively few companies.

But the rapid expansion of the industry brought an increasing measure of responsibility to the Federal Government. During the decade from 1910 to 1920, the development of long distance transmission resulted in the interconnection of water power plants with industrial and urban markets. The following decade saw the inter connection of steam generating plants, as well as water power plants and power markets. This marked a long step in the transformation of the electric utility industry from an aggregation of isolated local plants to large interconnected systems covering many States. These technical developments afforded lush opportunities for financial exploitation which reached its climax in 1929.

This expansion of the industry and financial exploitation exceeded the powers of the States to deal with it effectively.

One reason was the constitutional limitations spelled out in the court decisions. Another was the practical handicaps to effective regulation of the industry as operating companies were merged into larger aggregations and the capitalization, securities, and everyday operations and expenditures of operating companies were manipulated in disregard of local interests.

Signs of dangerous concentration of control of the vast utility industry, accompanied by corporate and financial abuses and expenditures of large sums of money to influence legislation and public opinion began to atone congressional suspicions that both consumers and the investing public were being victimized (69 Congressional Record 3022-23) Senator Thomas I. Walsh, of Montana, introduced a resolution authorizing an investigation, and in February of 1928 the (509) resolution was adopted which initiated the Federal Trade Commission's thoroughgoing investigation of the electric and gas utility industry.

Without waiting for the completion of that investigation, President Hoover on December 3, 1929, in his annual message to Congress recommended that a full time Federal Power Commission be created in place of the ex officio Commission composed of Cabinet officers which had originally been set up, and further, that the Commission's jurisdiction be broadened to include regulation of electric rates in interstate commerce where State commissions had no control.

Senator James Conzens, of Michigan, and Congressman James S. Parker, of New York, promptly introduced bills to carry out President Hoover's recommendations (S. 3869 and H. R. 11108, 71st Cong., 2d sess.). These bills were designed to give the Federal Power Commission jurisdiction over rates and charges for power sold in interstate commerce, over transmission of power in interstate commerce, and over other facilities or services furnished in connection with such a sale or transmission.

Congressman Parker, who was then chairman of the House Committee on Interstate and Foreign Commerce took the position in the debates on the bill that it was incumbent upon the Federal Government to regulate the interstate transactions in electric energy unregulated by the States, amounting at that time to 5 percent of the total electric energy used (72 Congressional Record 10333). The year 1930, however, saw only the administrative features of the bills enacted into law, while the enactment of substantive legislation awaited the report of the Federal Trade Commission investigation.

That report when completed in 1935 disclosed many evils which called for correction by legislation aimed at the holding company systems at levels above the operating companies. These disclosures led to the enactment of the Public Utility Holding Company Act of 1935, administered by the Securities and Exchange Commission. That act proceeded upon the principle that Congress has jurisdiction under the commerce clause to regulate the corporate and financial activities of holding company systems, because of the effect of those activities on interstate commerce, and not only interstate commerce in electric energy but also in securities.

But the Federal Trade Commission report also disclosed evils at the operating company level. These practices could be regulated by the Federal Government on clearly established constitutional principles because the bulk of the operating industry was comprised of the larger companies, most of which were engaged in part in interstate commerce. The Federal Trade Commission's report disclosed among other things, as recently summarized by its chairman:

1. That as a result of technological advances there had developed a large and increasing amount of interstate commerce in electric energy;

2. That this had been accompanied by an enormous expansion of interstate commerce in the stocks, bonds, and other securities of companies engaged therein;

3. That huge holding companies had gained and were exploiting their monopolistic control of such commerce carried on by their operating subsidiaries not only in production, transmission and sale of electric current but in the flotation and sales of securities on a wildly speculative basis;

4. That the resulting inflation of the capital structure of the industry had operated to inflate the rate base and the amounts paid by the consuming public for electricity; and

(510) 5. That all these unwholesome developments were beyond the effective reach of regulation by State utility commissions.

Many of the most serious abuses uncovered in the Commission's investigations were practices of misrepresentation and deception in financial matters through unsound accounting methods. This resulted in various forms of overstatement of capital assets, inflation of securities, and misrepresentation of income and surplus. The investigations disclosed large amounts of write up and inflation (Davis, Ewin L., The Influence of the Federal Trade Commission's Investigation on Federal Regulation of Interstate Electric and Gas Utilities, 14 George Washington Law Review 23).

The importance of correcting and preventing recurrence of such abuses at the operating company level is currently increasing as more and more electric utility companies are divested from holding company systems by the Securities and Exchange Commission. The twelfth annual report of that Commission discloses that, during the fiscal year ending June 30, 1916, 12 electric utility companies, with combined total assets of over $1,162,302,236, were divested by the SEC. In addition, 35 companies, with combined total assets of over

$1,891,271,757 were subject to divestment orders then outstanding. These companies will no longer be subject to regulation by the Securities and Exchange Commission as subsidiaries of registered holding companies, and in the future their corporate and financial practices will be subject, as the act now stands, to regulation by the Power Commission to prevent recurrence of the abuses of the past.

The purpose of Congress to go beyond the mere regulation of interstate wholesale rates and service and to use its constitutional powers over all companies engaging in interstate commerce in electric energy to remedy the abuses disclosed by the Federal Trade Commission, is plain from the provisions of part II and III of the Federal Power Act and from its legislative history.

Numerous provisions of parts II and III of the Federal Power Act are clearly not ancillary to or incidents of regulation of interstate wholesale rates or service. Among such provisions are those of section 305 (a), prohibiting officers and directors from profiting in the issuance and sale of utility securities and prohibiting payment of dividend out of capital: section 305 (b), restricting interlocking managements of electric utilities and underwriters or electrical equipment supplies: section 203 (a) regulating the sale, lease, or merger of facilities, and regulating the acquisition of securities of other companies; section 204, regulating the issuance of securities; and section 206 (b), authorizing investigation and determination of cost of service in certain cases where the Commission has no authority to fix rates.

The purpose to confer regulatory authority not limited to the regulation of interstate wholesale rates and service is also made clear by a comparison of section 208 with sections 301 and 302. While section 208 confers powers on the Commission to investigate and determine costs, depreciation, and other facts

"when found necessary for rate-making purposes," section 301 and 302 confer upon the Commission broad powers to regulate the accounting of the electric utilities subject to the act, not so limited.

That these regulations were all considered independent of the regulation of rates clearly appears from the legislative history of the act. The Senate report on the bill treats the regulation of wholesale rates as simply one among several purposes of the proposed legis-(511)lation (S. Rept. No. 621, 71th Cong., 1st sess. P. 18). It characterizes section 203 (a), providing for Commission control over the disposal, merger, or consolidation of facilities, as furnishing "an essential check upon the development of the industry along uneconomic lines." It referred to the section as complementing the Public Utility Holding Company Act of 1935–

by directing the Commission to prevent transfers or consolidation of property which would impair the ability of public utilities to render adequate service or impede, or tend to impede, the coordination in the public interest of facilities subject to the jurisdiction of the Commission id. p. 50).

Again, in explaining the Commission's control over the acquisition of securities of other public utilities, the Senate report stated that –

in this way the Commission would have authority to keep the same kind of check upon the creation of spheres of influence among operating companies that the Securities and Exchange Commission has over holding companies under title I.

At the hearings on the Federal Power Act, witnesses, including representatives of the utility industry, emphasized the importance of uniform and sound accounting regulation as an aid to the elimination of past abuses and the prevention of their

recurrence (hearings, House Committee on Interstate and Foreign Commerce, on H. R. 5423 (74th Cong., 1st sess.), pp. 345, 807-809, 1106-1107, 1307-1308, 1920). There was testimony by some witnesses that sound accounting alone was sufficient to cure the abuses (id. pp. 919, 1343) and the report of the Senate committee stated categorically that –

The authority of the Commission over the accounts of companies under its jurisdiction extends to the entire business of such companies (S. Rep. No. 621, 74th Cong., 1st sess., p. 53).

At attempt was made before the enactment of the act to amend the Federal accounting authority conferred by the act by providing that –

If, with respect to * * * the method of keeping accounts * * * any person is subject to the law of any State or regulation by a State commission, such person shall not be subject to the requirements (of the net) with respect to the same subject matter.

Although this amendment, offered on the floor of the House was adopted just before the vote on the bill in the House (79 Congressional Record 10574-10575), it was eliminated in conference (H. Rept. No. 1903, 74th Cong., 1st sess., pp. 63, 75).

At the House committee hearings on H. R. 5423, Dozier A. DeVane, Solicitor for the Federal Power Commission, and one of the original draftsmen of the bill (hearings, House Committee on Interstate and Foreign Commerce, on H. R. 5123 (74th Cong. 1st sess.), p. 515), made clear the independent importance of the provisions of the bill not relating to rates (id. P. 2170):

Mr. Hooker and every representative of the industry who has appeared before this committee has assumed that the sole purpose of title II of this bill is to regulate wholesale rates and their proceed to minimize the importance of or necessity for

such regulation. I do not have to tell the members of the committee that the actual fixing of rates is but a small part of the regulation sought to be accomplished by this bill. In the regulatory legislation which this committee has recommended and the Congress had adopted, more attention has been given to the character of service and facilities, the duties which must be performed, the construction, extension, and abandonment of facilities, the issuance of securities and the regulation of accounting than to the rate provisions themselves. I have already pointed out to you that every one of the regulatory provi-(512) sions in this bill has a clear analogy in the Interstate Commerce Act or the Communications Act. It was not until 1906, 19 years after the original Interstate Commerce Act was passed, that the Interstate Commerce Commission was given authority actually to fix a rate. It was not until 1920 that it was empowered to prescribe minimum as well as maximum rates.

Every single person so far as I know, who has appeared before you, has stated that power in one form or another should be conferred upon some regulatory agency created by the Congress to fix wholesale rates for energy transmitted in interstate commerce. Without minimizing in the least the importance of such legislation. I say to you this this bill should pass if it confers no authority over rates whatever and if for any reason Congress was compelled, which, of course, it is not, to choose between the rate provisions and the other provisions of this bill the public interest would be best served by enacting into law the other provisions of this bill.

During the debates, Representative Lea had this to say with respect to the independent purpose of the accounting provisions:

One of the most important features in this measure, as I view it, is that referring to accounts. The theory of this bill is to provide a unified accounting system for the public utilities of the United States. It would provide a common language for

accounting methods and meanings. It would help to standardize accounting methods and give stability and certainty to utility values (70 Congressional Record, 10378-79).

The Senate Committee in reporting the Federal Power Act pointed up the dual purposes of the act, when it said:

The decision of the Supreme Court in *Public Utilities Commission v. Attleboro Steam & E. Co.* (273 U. S. 83) placed the interstate wholesale transactions of the electric utilities entirely beyond the reach of the States. *Other features of this interstate utility business are equality immune from State control either legally or practically.* (Emphasis supplied.)

With such manifestations of the purposes of Congress, the Commission would have been derelict in its duty if it had not administered the act so as to accomplish those purposes. In carrying those purposes into effect every assertion of jurisdiction in hundreds of orders issued, with one exception, has been accepted, or if not voluntarily accepted has been affirmed by the courts. This unusual record makes it authoritatively certain that the Commission has not "attempted to grab power for itself by asserting jurisdiction over companies and activities never intended by Congress," has not misinterpreted "the laws of Congress in such a way as to give it the broadest possible field of jurisdiction without restraint;" and has not violated "the letter and spirit of the Federal Power Act."

In the one exception *The Connecticut Light & Power Co.* case, the United States Court of Appeals for the District of Columbia did affirm the Commission's order, but the Supreme Court caused the matter to be remanded to the Commission for further consideration. The case was unusual in the lengths to which the company went, even at some financial loss, to cut its interstate interconnections after the Commission had initiated proceedings against it. Two were cut while the proceeding was

pending and the cutting of the third and last was imminent when the Commission finally disposed of the case following the Supreme Court's remand.

THE EXEMPTIONS PROPOSED IN H. R. 2972

H. R. 2972, while not purporting to change the purposes of the Federal Power Act, actually does so. Congress can, of course, change those purposes. If that is to be done, however, there should be a clear

* * * *

(525) There is, however, a considerable difference between the proponents, as shown by their testimony here, and the Commission, in the understanding of just what the "Attleboro gap," so-called, was. We have the statement of the proponents that the gap consisted of sales at State boundaries between a company in one State and a company in another State. That is the kind of a situation which was involved in the Attleboro case, a sale by a Narragansett company at the State boundary between Rhode Island and Massachusetts, to a Massachusetts company. The Rhode Island company owned the transmission line right up to the State boundary and the Massachusetts company owned the continuation of the same line from there on to Attleboro. But the Attleboro decision in the principles which it applied and enunciated and the cases which it cited was not limited to a sale which is made at the State boundary.

It includes, in the first place, sales beyond the State boundary of electric energy moving from one State to another. That is made clear by the fact that the opinion in that case explicitly states that the point which the title to the energy passes is "wholly immaterial" and relies on *Missouri v. Kansas, Natural Gas Company* (265 U. S. 298).

There two States, Kansas and Missouri, had attempted to regulate the rates, which an interstate pipe line could charge in Kansas and Missouri, respectively, for gas which came in part from Oklahoma and in part from Kansas. The Supreme Court held that a State could not regulate the sale, at wholesale within its boundaries, of gas brought into the State from outside of the State, thereby making it perfectly plain that it is not only the sale at the State boundary, but the sale beyond the State boundary of a commodity–in that case gas–brought from out of the State which is beyond regulation by the State. The Supreme Court in the *Attleboro* case, where electric energy was involved, cited the gas case and applied the same principles.

Now, the proponents–and I do not want to violate the chairman's injunction against engaging in rebuttal, but much of what proponents say in a hearing like this throws light on the purpose of the legislation and I cannot deal with it without citing that. If I offend against what you think is proper, Mr. Chairman. I do not mean to, and I want you to stop me: but I think it will help in some instances to refer to it.

Mr. HALL. That will help us too. What I had in mind was going over their testimony item by item, taking some witness's testimony and going over it item by item, or taking each witnesses' testimony. You may proceed, and we will be very glad to have you comment on that.

Mr. WAHRENBROCK. That you. I thought that would be helpful.

Now, Mr. Brown at page 545 of the transcript said that wholesale sales after the first sale–assuming that the first sale was at the State boundary, or shortly beyond the State boundary–said that those wholesale sales after that first sale should be exempted. I assume that he implies that such sales are subject to regulation by the States.

The Supreme Court has had that problem before it in the case of gas–not in the case of electric energy–but the same principles

would apply. The case to which I refer is *Illinois Natural Gas Company v. Central Illinois Public Service Company* (314 U. S. 498).

I think these points can be understood if a part of my prepared statement can be referred to where I have the diagram illustrations. (526) That case is illustrated by diagram No. 5 on page 24 of my prepared statement (Tr. 1155) where we have an instance of a source of supply of electric energy in State X at (G) and the transmission line and generating plant is owned by company A. The transmission line from that generating plan crosses the State boundary into State Y, where there is a sale at wholesale to B. All B's facilities are located in one State, Y. B in turn sells to C within the same State and C locally distributes the energy.

Now, that is the type of situation which was involved in the *Illinois Natural Gas Company* case. There the Supreme Court held that the sale by B, all of whose facilities were located within the State of Illinois to C, was not subject to regulation by the State of Illinois, because the gas involved was gas which B had bought from a pipe-line company which brought it into the State from out of State.

Now, does the committee want to ask me any questions? My remarks are extemporaneous and I will be glad to respond as I go along or at the end of my statement.

MR. MILLER. I am not a lawyer. I am just wondering if the emphasis was on the pipe line, because there has been a good deal of discussion of that in this committee in connection with the gas hearings, and I wonder if the fact that the pipe-line company was a common carrier had any bearing.

Mr. WAHRENBROCK. I would say from my reading of those cases it makes no difference whether the commodity involved is natural gas or whether it is electric energy. I am not an expert on the Natural Gas Act, but I do not believe that the pipe-line companies were common carriers prior to the Natural Gas Act and I think it is a question, depending on what you mean, whether they are now. I doubt if they are now. They do have

certain obligations of public service which you commonly think of a common carrier having, but they are not made common carriers, as I understand it. However I am not as familiar with that act as the Natural Gas Act bureaucrats in the Federal Power Commission are.

Now, it is also clear from the *Attleboro* opinion that not only the sales at the State line and beyond the State line, but sales of electric energy *before* the State line is reached, are subject to the same principles which were applied in the *Attleboro* case. That is made clear by the citation in the *Attleboro* case of *Shafer v. Farmers Grain Company* (268 U. S. 189). There the commodity involved was wheat. The State had attempted to regulate the purchase of wheat and the conditions under which wheat was purchased by country grain elevators, which brought the wheat from farmers that drove in their with their wagons and dumped wheat into the elevator pits, and they, having processed the wheat, shipped it out into other States by common carriers.

There is was held that the attempt of the State to regulate those elevator operations–the conditions of those purchases of grain–was beyond its competence. The citation of that case, then, in the *Attleboro* case completes the picture, as it seems to me, from the legal point of view. Interstate commerce in electric energy, like that in gas and in wheat is beyond the power of the States to regulate beginning with the sale to the first purchaser, when the production is complete, continuing through the whole process by which it is carried out (527) of State to the point of local distribution in another State including the sale to the company which locally distributes. It was that gap in the power of the States to regulate which the Federal Power Act was enacted to fill.

The definitions of the act are explicit and carefully drawn so that the rate and service provisions of the act shall exactly plug the gap which those decisions had revealed. The Federal Power Act provides that the Commission shall have jurisdiction over companies that own or operate facilities for the transmission or sale at wholesale of electric energy in interstate commerce, but

shall not have jurisdiction over facilities for local distribution or generation or for transmission of electric energy consumed wholly by the transmitter or for transmission wholly in intrastate commerce.

MR. HALL. May I interrupt you to ask, did I understand you to say that the 1935 act was passed to close the so-called Attleboro gap and that purpose alone?

Mr. WAHRENBROCK. Not that purpose alone. I am discussing now the first of these two purposes, and we are in agreement with the proponents at least verbally, that that is one of the purposes. I am saying that in the regulation of rates and services the definitions have been so drawn as to exactly plug, and no more, the Attleboro gap. By this exemption of generating facilities, local distribution facilities, and the others that are mentioned in that "but clause." Congress exempted what had been excluded from the area which, in the cases culminating in the *Attleboro* case, the Court held was beyond the States.

The Supreme Court had held in tax cases–and they were cited in the history of the 1935 legislation–that generation was subject to State regulation, even though the energy was immediately sent out of the State. That was in *Utah v. Pfost:* It had held that local distribution was subject to regulation by the States, even though all of the energy distributed came from out of the State. Therefore, both of those exemptions were explicitly written into the act. Intrastate transmission–of course that was not a part of the gap so that was eliminated. Transmission of electric energy consumed wholly by the transmitter was obviously. I should suppose, a recognition of the holding of the Supreme Court in the so-called *Pipe Line Cases* where an oil pipe line company that took oil from one State to another for its own use was held subject to State jurisdiction. The definitions of the act were designed and drawn with care so that the rate and service provisions should exactly plug the gap which previous Supreme Court decisions had shown existed, and no more.

Now, so far as I am aware, there is no charge: no charge has ever been made, that the Federal Power Commission has ever

purported to regulate rates or services outside of that gap and Mr. C. W. Smith in his testimony will touch on that more fully.

I want now to turn to the second purpose of the Federal Power Act as disclosed by the legislative history.

Mr. MILLER. Pardon me, but do you intend to give us the second point in the *Attleboro* case? You said the first one was to close the gap and I believe that the chairman interrupted you there. I do not think I caught the second one.

(528) Mr. WAHRENBROCK. Now, I am not sure that I know what you refer to. I was not going to make any further point about the *Attleboro* case. I was going to give what we had regarded as the second purpose, general purpose, of the 1935 legislation.

Mr. MILLER. I misunderstood you. I thought that you were referring to the *Attleboro* case when you referred to the second point.

Mr. WAHRENBROCK. The *Atteboro* case actually held a sale at the State line beyond the power of the State to regulate and it relied upon cases including both cases beyond the State line and cases prior to the State line and said that it made no difference at what point the title passed, that so long as the electric energy or oil or gas was moving in interstate commerce, it was beyond the power of the State to regulate beyond the point of generation and up to the point of local distribution.

Mr. MILLER. You said that the 1935 amendments were adopted first of all to close the gap pointed out in the *Attleboro* decision?

Mr. WAHRENBROCK. Yes, sir.

Mr. MILLER. And for some other reason, a second reason.

Mr. WAHRENBROCK. Yes: I will mention those now.

Mr. MILLER. I did not know whether you had forgotten that or not, I am sorry.

Mr. WAHRENBROCK. I am glad to have an opportunity to make that plain, because while there is at least verbal agreement among the proponents and ourselves apparently with respect to the filling of the Attleboro gap, the proponents of this

legislation, in their testimony here have either overlooked or denied the existence of what we believe to be the second purpose of this legislation, and that was to correct the corporate and financial abuses in the utility industry which had been disclosed by the Federal Trade Commission investigation.

Mr. HESELTON. Did you say second or secondary?

Mr. WAHRENBROCK. I did not say secondary. The Supreme Court has characterized the filling of the Attleboro gap as a primary purpose.

Mr. HESELTON. I wanted to get your exact expression.

Mr. WAHRENBROCK. I said second. The Supreme Court has not excluded other purposes as being of equal importance. It has referred to this one as a primary purpose, the filling of the Attleboro gap as a primary purpose.

Mr. HESELTON. May I interrupt you there again, because I have made a note and you now for the second time I think have said in the record "a" primary purpose. Was it "a" primary purpose or "the" primary purpose?

Mr. WAHRENBROCK. I am glad you asked that. The Court uses "the primary purpose."

Mr. HESELTON. And that is repeated in the *New Jersey* case and *Connecticut* case?

Mr. WAHRENBROCK. That was used in the *New Jersey* case first by Mr. Justice Reed.

Mr. HESELTON. And reaffirmed in the *Connecticut* case?

Mr. WAHRENBROCK. And quoted by Mr. Justice Jackson in the *Connecticut* case. It is interesting to note that in the *Jersey Central* case Mr. Justice Reed used it in writing an opinion which affirmed the jurisdiction of the Commission over a company which the Commission had found owned facilities for transmission of electric energy. The

* * * * *

(548) Mr. HESELTON. I want to refer again and want your reaction to this specific quotation from the hearings in the House

where it is said that the first objective of the bill is a complement to State regulation of rates. As a part of that complement the bill provides that the Federal Power Commission may regulate the rates that no State commission can regulate.

Mr. WAHRENBROCK. That is right.

Mr. HESELTON And the bill simply fills this gap, and that is all.

Now, that is pretty emphatic language.

Mr. WAHRENBROCK. May I make this plain. What is there being talked about–and I think you will agree with me–is a regulation of rates.

Mr. HESELTON. That is right.

Mr. WAHRENBROCK. And no one charges before this committee or any place else that the Federal Power Commission has ever issued any rate of service order which has encroached on any rate or service which the State had constitutional power to regulate. No one has ever charged that. The fact of the matter is that Mr. Benton, in the George Washington Law Review article referred to, himself says that that is the fact: that we have never gone beyond that. That has been recognized clearly. There is no question about that.

Mr. HESELTON. All right. My next question is, Why does not all of the testimony we have in the hearings indicate the same intention? It is reported over and over again, and I read from the record yesterday, that it was the intention of Congress at that time to supplement and assist the States and not oust them from jurisdiction.

Mr. WAHRENBROCK. That is right. Now, that is exactly what I have been saying. I think you and I have a little bit of difference in our minds, but the wording is the same, and I want to point out what I said earlier–I think you were not in the room when I said it–that the second purpose was to prevent corporate and financial abuses by supplementing State regulation in the field in which the States legally might have the power but which those very reports–and I read one of them when you were not

here, the report of Senator Wheeler–pointed out that the States had not as a legal or practical matter effectively regulated the companies within the States.

Mr. HESELTON. I want to ask one final question and then I am through.

You do not contend that the Securities and Exchange Commission does not do an effective job, do you?

Mr. WAHRENBROCK. I am glad you brought that up, because there was one reference to it previously and there seems to have been in the minds of some of the members of the committee that there is possibly a field in which there might be overlapping between the Federal Power Commission and the Securities and Exchange Commission.

Section 318 of the Federal Power Act effectively prevents that. It says that whenever a person is subject to a requirement of the Public Utility Holding Company Act or of any order, rule, or regulation thereunder, it shall not be subject to any requirement of the Federal Power Act or any order, rule, or regulation under that act with respect to the same subject matter.

Now, as the Securities and Exchange Commission breaks up the holding company systems and turns loose the independent companies,

* * * * *

(551) Now, the sale of the Western Massachusetts Co. to the Middletown Co. is made at the State boundary.

What I was just trying to say was that the transmission line from the Massachusetts boundary to Middletown, where the local distribution takes place, is a transmission facility which it was one of the purposes of the framers of the Federal Power Act to provide, should be available for interstate use and service. The State of Connecticut could not tell the Middletown Co. to serve Hartford or to serve Taftvale, or any of the other communities along the route, if the companies in those communities needed service; if in a wartime emergency they

needed the power that was available on that high tension line, and because of a competitive relationship they could not get it by bargaining.

Now, section 202 (b) of the Federal Power Act gives the Federal Power Commission the authority, on the application of the State commission or the application of a private company to compel that interstate company to serve others who may want service.

Mr. MILLER. You say that the Connecticut commission could not compel them to serve any company or any community in Connecticut?

Mr. WAHRENBROCK. That is right. That is interstate transmission. That follows from the principles of the Attleboro case.

Mr. HALL. Let us assume that Congress said that it was not an interstate line from the Connecticut border.

Mr. WAHRENBROCK. Congress cannot say that. What is interstate commerce is interstate commerce.

Mr. MILLER. It is not interstate commerce though.

Mr. HALL. In other words, that is the Attleboro gap?

Mr. WAHRENBROCK. That is within the Attleboro gap.

That is what I meant to point out in connection with the Central Illinois Public Service Co. case to which I referred earlier (314 U. S. 498). There was a case in which, and I am glad you asked that question, because I did not make that aspect of that case clear, there was a case in which the Illinois Commission tried to compel service by a company, all of whose transmission was just exactly that of the Middleton Co. It bought, not at the State line, but inside the State, and the Commission tried to compel that company to serve a local distributing company in the State, and the Supreme Court held that that effort was unavailing and they struck down that order. That is then part of the Attleboro gap.

In spite of my efforts to get forward, and I may not seem to have been succeeding, but I have been trying, I am using more time than I had expected and if the committee is going to

adjourn today I want the witnesses that follow me to have some time. I have only covered the first exemption. I have five to go. They will not take quite as long, but I do have more. I wonder if I ought to raise that question as to how much time is left and where we are.

Mr. HALL. I am going to finish this with one more hearing. Everybody will have to condense in order to finish. In other words, that means that we will have no more than 2½ hours, and I think by that time the committee will have been very generous with both sides of the case.

Mr. MILLER. Before you leave that, you way that this language in 2972 which we have discussed, contrary to what he proponents say, (552) does leave a gap. I do not care whether it is the Attleboro gap or not, but it leaves a gap that cannot be controlled by either the State or Federal Government. That, briefly, is the picture?

Mr. WAHRENBROCK. That is right.

Mr. HESELTON. I am confused. I have the syllabus in the Attleboro case before me. I had always understood that the difficulty there lay in the inability of the State of Rhode Island to regulate the transmission of the energy to the line in Rhode Island and that there was no concern as to the regulation over the transmission from the Rhode Island line into Massachusetts. In other words, the Chairman has placed the emphasis in his example on the ability of Connecticut to regulate transmission from the State line down into Connecticut, and you have turned this around and said that it is analogous to the Attleboro case, when, as a matter of fact, it seems to me it is not.

Mr. WAHRENBROCK. I think what has given rise to the difficulty here is this: You are right. In this aspect of the Attleboro case, the Rhode Island commission sought to prevent the Narragansett Co. from charging its affiliate in Massachusetts a low price for the energy that was shipped up to Massachusetts. It said that is so low that our citizens are being discriminated against and our citizens are having to pay a higher rate. It,

therefore, attempted to increase that rate. The Supreme Court said, "That is outside of your power to do."

Mr. HESELTON. Using the chairman's example, that would be as though the Massachusetts Public Utilities Commission attempted to do that and found that it could not under the Attleboro decision, but it does not decide the question as to the control by the Connecticut commission over the rates within intrastate commerce in Connecticut. Am I right about that?

Mr. WAHRENBROCK. I am applying the principles that were relied on in deciding the Attleboro case and were subsequently applied by the court in this Illinois case to which I have referred and not merely the limited holding in the Attleboro case. I think you are thinking of the immediate holding in that case only.

In the Central Illinois Public Service Co. case there was not only the regulation of the rate, but, also, the regulation of service.

This first exemption is not conferred merely by one clause, but there are two clauses. There is the language which appears in lines 7 to 12 on page 2 of the bill, which apparently is intended to accomplish something of the same thing. What makes it extremely difficult from the point of one who views this, as I do, in attempting to see how it would be enforced, is to understand why it is necessary to write two provisions to accomplish the same purpose. When that is done, it begins to look as though there is more than one purpose in mind and makes one seek to ascertain why duplicating language is necessary to accomplish one purpose.

The second exemption is that which appears on page 3, lines 2 to 10. That is where energy, generated in the State, is sold to another company which takes part of it out of the State, unless the principal purpose of the sale is the transmission out of State.

This was stated by Mr. Brown at transcript 536 as being designed to obviate such situations as the Jersey Central situation. Again, we have duplicate provisions to accomplish the same thing, because the type of provision which appears on page 3, lines 11 to 20, is stated

* * * * *

(553) by Mr. Brown, also, to be aimed at the same type of situation, that is, the exemption of exchange agreements or arrangements which are for emergency energy or economy energy or involve only a slop-over.

Mr. HESELTON. That is the slop-over provision in that section.

Mr. WAHRENBROCK. I think that is probably the least important part of it, but I am pointing out now that there are these duplicate provisions both of which are explained as being intended to deal with the Jersey Central problem.

Mr. MILLER. There was a good deal of discussion as to why that language is duplicated. It would seem to me that they were saying the same think, but in the testimony that was explained. All I can say is that I will have to look up the reason again, but I thought, as you did, it seemed funny to put that in twice, but there was a reason given that seemed perfectly reasonable and harmless to me.

Mr. WAHRENBROCK. If one is adequate for the purpose which the proponents of the legislation state, and I am speaking of Mr. Brown in particular, the one that they urged, that he included, I do not see why it is necessary to add the other for the same purpose.

Mr. MILLER. There is a good reason for that. I will look it up this evening.

Mr. WAHRENBROCK. From the point of view of one who has attempted to prove these matters, to establish them by examination of witnesses, by documentary evidence, I might say that this qualification involving the principal purpose might just as well not be there. I mean the principal purpose of the sale. Because I think any of you who are lawyers will appreciate that it is going to be impossible, practically impossible, to prove the principal purpose. You have to determine the mental purpose of people and do that when all of the incentive to them is not to disclose their purpose, or if anything, to disclose some other

purpose. To get proof of principal purpose is going to be impossible. That is an unworkable exception. And it just simply, then, stands as a practical matter that where the energy is sold and part of it goes out of the State and the whole sale is exempt. That again is to exempt a sale which is beyond the power of the States to regulate, even as to the sale price. A State cannot regulate the price charged for energy that is going out of the State whether it is before the State line is crossed or after. So here is a case where again the Attleboro gap with respect to rates and service itself is re-created literally and the purpose to protect against financial and corporate abuses is weakened and broken down so far as companies are by this exemption eliminated.

Mr. MILLER. I did not get the language that you are discussing.

Mr. WAHRENBROCK. I am discussing the sale where part of the energy goes out of the State.

Mr. HESELTON. Section 2.

Mr. WAHRENBROCK. That is page 3, lines 2 to 10.

I want to point out that the result of the Jersey Central case is not to bring within the Commission's jurisdiction any company within the State which is interconnected with another company that has out-of-State connections, the result of that case is not to make every such company subject to the jurisdiction of the Federal Power Commission. Mr. Justice Reed, in his opinion in the Jersey Central case, dealt with the very contention which was advanced by the company there, and (554) he said in that case, "Mere connection determines nothing." What has to be ascertained, and what he said had been ascertained, and which he found substantial evidence to support, is that there was energy generated in one State which was transmitted over the facilities of the Jersey Central Co. and transmitted from that State and consumed in another State. The effect of that is that if you exempt that kind of transaction, there is a transaction which is within the Attleboro gap which is taken out of regulation again. There is not a single one of these exemptions which does

not re-create the Attleboro gap as to rates and service as well as destroying the second purpose.

I say a single one, that does not apply to the immunity provision. That is one of them.

Mr. MILLER. By gap you mean that they would be controlled by neither the State nor the Federal Government?

Mr. WAHRENBROCK. That is right.

Mr. HESELTON. As one member of this committee I have no desire to see any legislation that leaves any company unregulated. I think that the gap should be completely filled, and I think, although you are making a splendid statement, you are wasting your energy on me.

Mr. MILLER. Likewise.

Mr. WAHRENBROCK. Maybe I am not. If I can point out that it is not merely a question of exempting a company, but of exempting transactions. These companies may, as to many transactions, be subject to State regulation, but I am calling your attention that as to the particular type that is being exempted, they will not be. Do I make that point clear?

Mr. HESELTON. Again, I thank you for that statement.

Mr. MILLER. Before you leave that, what public interest is involved in that second amendment to subsection (c)?

Mr. WAHRENBROCK. Just what Mr. Justice Reed referred to in the Jersey Central case. If the Jersey Central Co., which transmits energy and delivers it to the Public Service Co., which, in turn, delivers part of that energy into New York and there sells it, if the Jersey Central Co. can fix a rate, a high rate, for that energy, then the Public Service Co., which resells that across to a New York company, has to pass on that high rate, and the State of New York which is interested in protecting its consumers against high rates is powerless to do so because the increment of cost is beyond its power to control.

Mr. MILLER. Suppose the circumstances were reversed because of the interconnection, you might be able to get their power from some company such as you have outlined that has

peak capacity at a lower rate. That might go the other way. It would give them a reduced cost.

Mr. WAHRENBROCK. That is right. And the jurisdiction that is given to the Federal Power Commission is to assure that every advantage of such reduced cost shall inure to the benefit of the consumers in other States.

The next exemption is that a company in one State shall not be a public utility by interconnection with a Government agency. That is on page 5 of the bill, lines 1 to 11.

Mr. Brown said that was to exempt situations like the Connecticut Light & Power Co.'s sale to the borough of Groton.

If that is the purpose as Mr. Brown said it was, then we have the case again of a duplicate provision because the sale to the borough (555) of Groton falls exactly within the preceding exemption, that is, the principal purpose exemption, and it seems remarkable that three or four necessities of the Connecticut Light & Power case and the Jersey Central case should give rise to so many overlapping and duplicative provisions, if that is the only purpose intended.

MR. MILLER. Why do you take Mr. Brown's opinion as to the interpretation of the legislation. I do not know the gentleman; I have never talked to him. I certainly know that he has never talked to me about the bill. That is four or five times that you have taken his particular statement, his interpretation, as your authority.

MR. WAHRENBROCK. I want to be perfectly frank as to why I did that; that is, the reason I did that. As I went over the statements of the proponents of the bill, Mr. Brown and Mr. O.D. Smith were the only two lawyers, the only two men, who explained the purposes of the provisions in detail, and Mr. Brown time and again said, "This exemption is designed to do this." No one stood up here and said he had drafted this bill. Mr. Benton assumed responsibility for the Boren bill, and so far as the language in part of this act corresponds to that, I suppose the authorship is apparent.

FEDERAL POWER COMMISSION.
Washington 25, June 13, 1947.

HON. CHARLES A. WOLVERTON,
Chairman, Committee on Interstate and Foreign Commerce,
United States House of Representatives,
Washington, D.C.

MY DEAR MR. CHAIRMAN: In response to your request, the Federal Power Commission submits this report on H. R. 2972. This bill would amend part II of the Federal Power Act by providing exemptions for a majority of electric utilities now subject to regulation under that part of the act. That regulation extends to interstate wholesale electric rates and to certain corporate and financial practices of companies having facilities for interstate commerce in electric energy.

The first Federal regulation of this nature, provided by the Federal Water Power Act of 1920, was limited to a comparatively few electric utilities which had hydroelectric projects on public lands or involving navigable waters of the United States. But during the decade following 1920 there was a rapid growth of transmission networks interconnecting water-power and steam-generating plants and local distribution systems. This development constituted a long step in the transformation of the industry from an aggregation of isolated local plants to large interconnected systems covering many States.

As a localized industry, electric utilities had long been subject to local regulation, but in the expansion of the twenties the industry outgrew such regulation because of the practical difficulties and constitutional limitations which handicapped individual States. Toward the end of the decade Congress and the Executive became concerned over the need for Federal action, and the steps they then took led directly to enactment of the 1935 legislation.

While H.R. 2972 does not purport to amend any of the regulatory provisions of that legislation, the sweeping nature of the exemptions which it proposes would leave only a handful of

companies to be regulated. The bill therefore must be viewed as a substantial repeal of the regulation itself.

THE PROPOSED EXEMPTIONS WOULD BE A VIRTUAL REPEAL OF THE ACT

Congress, in section 201 of the Federal Power Act, described the electric utilities to be regulated as companies owning or operating facilities for the transmission, or sale at wholesale, for electric energy which is transmitted from any State and consumed outside thereof. Facilities used for generation, or in local distribution, or only for intrastate transmission, etc., were excluded. In addition, certain activities of companies otherwise subject to regulation were exempted. As the House Committee on Interstate and Foreign Commerce said:

> "The bill takes no authority from State commissions and contains provisions authorizing the Federal Commission to aid the State commissions in their efforts to ascertain and fix reasonable charges. Provision is made for joint boards composed of members of State commissions which may be used for this purpose. The new parts are so drawn as to be a complement to and in no sense a usurpation of State regulatory authority and contain throughout directions to the Federal Power Commission to receive and consider the views of State commissions. Probably no bill in recent years has so recognized the responsibilities of State regulatory commissions as does title II of this bill."

The exemptions in the proposed bill, however, would go much further than the present statutory provisions limiting the scope of Federal regulations to (333) the extent of wholly disregarding the recognized needs which gave rise to this

Mr. O.D. Smith said that he only "helped them," and I do not know who "they" are, in the drafting of the bill.

When Mr. Brown said, "This provision is designed for so-and-so," and "this other provision is designed for so-and-so," and no other proponent purported to state what the purposes of these several provisions are, I naturally took that as the proponent's statement of what the bill was designed to do.

MR. MILLER. I assume full responsibility for the language, although I did not draw it, of course, but I went to the people who did as a result of correspondence that I knew indicated they had problems and tried to find out what their difficulties were, and there were half a dozen different people who contributed to the language and gave their thought, and the committee has before it 12 or 15 amendments to these 2 bills that have been submitted to us for consideration.

MR. WAHRENBROCK. I will make one final comment about this exemption of a company wholly in one State that it shall not be a public utility by reason of interconnection with a Government agency.

If a company by interconnection with a Government agency transmits or sells at wholesale any energy which goes out of the State and is consumed in another State or which comes from another State and is consumed in the first State, then that company is exempt from State regulation of that energy transmission in interstate commerce and the sale and wholesale in interstate commerce within the Attleboro gap, regardless of whether it comes and crosses the State boundary on Government facility or not. So this exemption, too, recreates, so far as it extends, the Attleboro gap with respect to the regulation of rates and service as well as destroying or withdrawing the safeguards against the financial and corporate abuses that I spoke of.

MR. MILLER. What would the situation be in the case of an intrastate company not now regulated by the Federal Power Commission that sold electrical energy to the city of New Haven, to use that as any illustration, and we will assume that it is a city-owned plant, the city plant in New Haven sells

electricity and runs a line across to Fisher's (556) Island, N.Y. What effect would that action have on your control of the intrastate company in Connecticut?

MR. WAHRENBROCK. You said an intrastate company not now subject to our jurisdiction. On the facts you have given, that company would not be subject to our jurisdiction.

MR. MILLER. That is what I want to get. The mere fact that they sold to a municipally owned company plant, and that plant in turn sold to Fisher's Island, which is owned by New York.

MR. WAHRENBROCK. That is energy which is transmitted from a State and consumed at a point outside thereof. Under the Attleboro and the preceding cases, the States are powerless to regulate the rate of that sale to the city of New Haven, and if you exempt that sale from Federal regulation, it is put in the no man's land of regulation.

MR. MILLER. As I understand, that was the situation that they attempted to cure.

MR. HALL. Do you think that if an amendment like this was placed in this bill it could cure that situation:

It is hereby declared to be in the public interest that the business of generating, transmitting, and selling electrical energy for ultimate public consumption shall be subject to public regulation, and to the extent that such business is not subject to the jurisdiction of the Commission under this act the same is hereby declared to be local in character and shall be subject to regulation by a State authority.

MR. WAHRENBROCK. That is the question which you asked me to be prepared to answer. That is Mr. Benton's amendment which would add a section 6 to H.R. 2972, and that in turn would add a subsection (g) to section 201.

The thing that concerns me in the first place about that is when it says, "by State authority," and the question which is immediately raised by that is authority of what State? Take your Attleboro case, it was there to the interest of Rhode Island to keep that rate high. It was there to the interest of Massachusetts to keep that rate low. Depending on which State authority you are going to have a tendency for a high or a low rate. If it is the

State authority in the State of production, the tendency will be a high rate. If in the State of consumption, the tendency will be a low rate. You have that conflict.

MR. HALL. Do you think that one State public utility will charge excessive rates to another State public utility?

MR. WAHRENBROCK. Well, in the absence of regulation, what is to prevent that?

MR. HALL. Where both of them have commissions?

MR. WAHRENBROCK. What incentive is there for the State of production to cut down the price which its citizens may receive from the citizens of another State?

MR. HALL. Do you think they will charge a rate which is all out of line with the rates that are charged to its local citizens?

MR. WAHRENBROCK. That, I submit, is a practical question for Congress.

MR. HALL. That is quite a lack of faith in cooperation between States, I would say.

MR. WAHRENBROCK. I do not think it implies lack of faith to say that utility rates need be regulated. I am pointing out here that the regulation is not by the State of the consumer which is the State that is interested in securing regulation. Regulation is expensive, (557) it is difficult, it requires prodding by the public that is interested in it. It should be responsive to the public upon whose behalf it is instituted. This conflict between he interests of the State of production and the State of consumption is essentially the problem which gave rise to the commerce clause. That is the reason we have a commerce clause. That is the reason in these cases which culminated in the Attleboro case the Supreme Court held that in the silence of Congress, with no attempt by Congress ever to regulate this industry, the States still could not regulate it. Now, that being true, I have considerable doubt that the case upon which Mr. Benton relied and which involved the continuation of a tax of insurance companies—a tax on aggregate premiums within a State, a matter which had traditionally been held to be within the power of the States in the silence of Congress—I have grave doubts whether that case, despite the breadth of the language of the

opinion, would be held to apply to validate discriminatory State regulation of rates.

MR. HALL. Have you any examples which would show that in the period before the enactment of the Federal power legislation one State commission would approve exorbitant charges for power generated in the State and sold to utilities in another State?

MR. WAHRENBROCK. The reason no such example can be cited is that the states were held not to have power to regulate those rates.

MR. HALL. Do you know of any example where the rates were exorbitant?

MR. WAHRENBROCK. Well now, as a lawyer I have not attempted to familiarize myself with rates and what the practices have been.

In connection with the question about Mr. Benton's amendment, Mr. Chairman, I would like to call this committee's attention, as probably I do not need to, to what this committee has recently said on that question in its report No. 800 of this Congress, this session, to accompany H.R. 4051, the Rizley bill. I refer to pages 10 and 11 of that report, where this committee in talking about the Rizley bill said:

The bill makes no change in the present law as to direct sales by pipe lines to industrial consumers which sales under the Natural Gas Act are exempt from Federal Power Commission jurisdiction. Your committee feels that no change is necessary in the public interest. Your committee has considered the amendment offered by the National Association of Railroad and Utility Commissioners proposing to permit the various States to exercise jurisdiction over direct sales and has concluded that the adoption of the amendment would not be in the public interest, but would be more likely to add to the existing confusion.

That was a similar, although more limited proposal, to that which you have just read to me, and here is what your committee says, and I read two or three sentences—

Your committee feels that to alter—

MR. HESELTON. You omitted one rather significant sentence.

MR. WAHRENBROCK. I have skipped a sentence.

MR. HESELTON. That sentence is:

That pipe line does not occupy a utility status with reference to direct sales.

That is what we are talking about in the paragraph, is it not?

MR. WAHRENBROCK. I recognize that. What I am going to say now does not indicate or does not represent a feeling on my part that what

* * * * *

APPENDIX N

Hearings Before the Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce House of Representatives 80th Congress, 1st Session, (1947), excerpts from Testimony Nelson Lee Smith, Chairman, Federal Power Commission

N-1

FEDERAL POWER ACT

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE COMMITTEE ON

INTERSTATE AND FOREIGN COMMERCE

HOUSE OF REPRESENTATIVES

EIGHTIETH CONGRESS

FIRST SESSION

ON

H.R. 2972

A BILL TO AMEND SECTION 201

OF THE FEDERAL POWER ACT

AND

H.R. 2973

A BILL TO AMEND

THE FEDERAL POWER ACT

JUNE 23, 24, 26, JULY 2, 10 AND 11, 1947

Printed for the use of the
Committee on Interstate and Foreign Commerce

AMENDMENTS TO FEDERAL POWER ACT

WEDNESDAY, JULY 2, 1947

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE OF THE COMMITTEE ON
INTERSTATE AND FOREIGN COMMERCE.
Washington, D.C.

(331) The subcommittee met at 10 a.m., pursuant to call in room 1334, New House Office Building, Hon. Leonard W. Hall (chairman of the subcommittee) presiding.

Mr. Hall. The committee will come to order

We are resuming hearings on H. R. 2972 and H. R. 2973.

The purpose of the meeting this morning is to hear representatives of the Federal Power Commission.

STATEMENT OF NELSON LEE SMITH

Mr. Hall: Mrs. Smith, I understand that you have a short statement which you wish to make.

Commissioner Smith: Mr. Chairman, that is correct. My name is Nelson Lee Smith. Since the autumn of 1913 I have been a member of the Federal Power Commission, and on January 1 of this year I became its chairman. Previously I had served for nearly 8 years as chairman of the Public Service Commission of the State of New Hampshire, and in 1939 was president of the National Association of Railroad and Utilities Commissioner. I do, as the chairman has stated, wish to make a very brief general statement as an introduction to the Commission's presentation in opposition to H. R. 2972 and H. R. 2973.

There have been some rather regrettable references on this record to the greed for power of the Federal Power Commission and to a voracious appetite for authority which as led to its rapaciously reaching out and grasping for jurisdiction. At the outset I want to make it clear that the Federal Power Commission is well aware of the fact that it is an arm of the Congress, which created it. It possesses only the powers and duties which Congress has by statute given it. The Commission understands that its job is to administer and apply to particular situations the national policies which the Congress has laid down. In so doing it has an obligation to adhere scrupulously to the congressional intent.

When changes in the congressional instructions which govern our work are suggested, however, we believe—and I am sure you will agree—that it is our duty to present the results of our experience and our judgment regarding the effects of the proposed amendments. (332) In matters of this character and importance appeals to emotion or prejudice should, like personalities, have no place. The problem is an intellectual one, which calls, not for heat or feeling, but for light and for dispassionate analysis to disclose the merits of divergent positions.

It has been stated that the purpose of these bills is to clarify certain particular situations. In response to the committee's request, the Commission on June 13 filed reports on each of the two bills here under consideration, which I suppose have already been made a part of this record.

(The reports above referred to are as follows:)

legislation. The sweeping scope of those exemptions is apparent from a brief statement of their effect.

Under H. R. 2972. any company, now subject to regulation under part II because of its ownership or operation of facilities for transmission or sale at wholesale of electric energy in interstate commerce, would be exempted:

(1) If none of its facilities cross State boundaries and if the company also engages in local distribution (Sec. 2. p. 2, line 20. to p. 3, line 2); or

(2) Regardless of whether such facilities cross State Boundaries, if any sale or sales at wholesale of such energy are made in the State within which the energy is consumed, and if the company is also engaged in local distribution wholly within any one State. (Sec. 2, p. 2, line 20, to p. 3, line 2: this provision, although very confused, apparently would remove transmission facilities across State boundaries from Federal regulation in instances where the company's distribution facilities are located wholly in one State, thus going beyond the exemption provided in sec. 1 of the bill): or

(3) If by means of such facilities it transmits and sells at wholesale locally generated energy to a person transmitting a part thereof to another State, provided the purchaser is engaged in local distribution within the first State and the principal purpose of the sale is not transmission out of the State (sec. 2, p. 3, lines 2 to 10): or

(4) If the energy, which it transmits or sells at wholesale in interstate commerce, is exchanged and settlement therefor is made on a cost basis (sec. 2, p. 3, lines 11 to 20).

In addition:

(5) Any transmission or sale of electric energy in interstate commerce to or from a governmental agency

would not subject a company to the provisions of the Federal Power Act (sec. 5, p. 5).

(6) No sale of electric energy at wholesale in interstate commerce would remain subject to Federal regulation except where not only the seller but also the buyer would be subject to the narrowed jurisdiction of the Commission under the amendments. This exemption would include all sales to intrastate companies and all sales at the beginning of interstate commerce. (This is due to the provision that for a wholesale sale of electric energy to be one "in interstate commerce" it must be "in the course of transmission of such energy in interstate commerce as defined * * *" (sec. 3, p. 3, line 21, to p. 4, line 2) which apparently has the effect of requiring that both the buyer and seller must transmit the energy "in interstate commerce" under the narrowed meaning given that term.)

(7) Any company subject to any regulation by the act could violate the regulation and avoid being compelled to comply by ceasing to be a "public utility" under the act, either as a result of the taking effect of the amendment or by termination of the operations which would otherwise still subject it to the Commission's jurisdiction under the amended act (sec. 4, p. 4). Apparently also it could avoid the penalties for its violation the same way. There appears to be no obstacle to the resumption of the interstate operations as soon as the threat of enforcement has passed, permitting the company to play hide and seek with the Commission.

A check of available data indicates that, as a result of the enactment of the bill, at least three-fourths of the companies now subject to Commission regulation would be excluded. It is also apparent that the large number of overlapping exemptions and the difficulties of interpreting the act with the added provisos, escape clauses, and other exemptions, would multiply

the grounds of litigation and seriously complicate the administration of the act as to the companies which would remain subject. At the same time the numerous possibilities of easy escape would make it probable that in the everyday administration of the act the public interest would come off second best when it conflicted with the private interests of the affected utility.

HISTORY AND PURPOSES OF PART II

The Federal Water Power Act of 1920, forerunner of Part II of the Federal Power Act, as already indicated, dealt only with a comparatively few companies. Municipal and State regulation of electric utilities had developed early because they were engaged in public service: they enjoyed special privileges, were recognized as a practical monopoly, were given a protected market, had delegated to them the sovereign power of eminent domain, and were given the use of public (334) streets and highways. But as the industry grew and spread, interstate transmission of electric energy increased, taking it more and more out of the regulatory powers of the States and creating a situation in which many phases of utility activity could be reached only by congressional action.

This was emphasized in 1927 by the important decision of the Supreme Court in the Attleboro case, striking down an attempt of the State of Rhode Island to regulate rates which an electric utility in that State charged an affiliated Massachusetts company and which the Public Utility Commission of Rhode Island thought discriminated against consumers in Rhode Island.

In addition to constitutional limitations, individual States encountered increasing practical handicaps to effective regulation of the industry as operating companies were merged into larger aggregations and their capitalization, securities, and everyday operations and expenditures were manipulated in disregard of local interests. Warning signs of possible financial and corporate abuses began to be discerned which caused the

Congress in 1928 to initiate a comprehensive investigation of the utility industry by the Federal Trade Commission.

Even before that investigation was completed, President Hoover, in his annual message to Congress, December 3, 1929, recommended the enactment of legislation reorganizing the Federal Power Commission as an independent agency and providing Federal regulation to supplement State regulation of electric utilities.

A month later Senator Couzens of Michigan introduced a bill which went further than the President's recommendations and embodied many of the provisions found in the present law. Only that part of the bill providing for the reorganization of the Commission was enacted into law that year, however. Substantive legislation awaited the report of the Federal Trade Commission investigation.

The Federal Trade Commission report, when completed in 1935, disclosed among other things, as stated by its Chairman:

> "(1) That as a result of technological advances there had developed a large and increasing amount of interstate commerce in electric energy:
> "(2) That this had been accompanied by an enormous expansion of interstate commerce in the stocks, bonds, and other securities of companies engaged therein:
> "(3) That huge holding companies had gained and were exploiting their monopolistic control of such commerce carried on by their operating subsidiaries not only in production, transmission, and sale of electric current but in the floatation and sales of securities on a wildly speculative basis:
> "(4) That the resulting inflation of the capital structure of the industry had operated to inflate the rate base and the amounts paid by the consuming public for electricity: and

"(5) That all these unwholesome developments were beyond the effective reach of regulation by State utility commissions."

His statement continues:

"Many of the most serious abuses uncovered in the Commission's investigations were practices of misrepresentation and deception in financial matters through unsound accounting methods. This resulted in various forms of overstatement of capital assets, inflation of securities, and misrepresentation of income and surplus. The investigations disclosed large amounts of write-up and inflation. The capital assets of the holding and operating companies examined in the electric utility industry were written up in value over cost in one way or another by more than $1,400,000,000. * * *" (Davis, Ewin L., The Influence of the Federal Trade Commission's Investigation on Federal Regulation of Interstate Electric and Gas Utilities, 14 George Washington Law Review 23.)

In reporting the Federal Power Act the Senate Committee on Interstate Commerce, after referring to the increase in the proportion of electric energy crossing State boundaries from 10.7 percent in 1928 to 17.8 percent in 1933, said:

"The decision of the Supreme Court in *Public Utilities Commission v. Attleboro Steam & E. Co.* (273 U.S. 83) placed the interstate wholesale transactions of the electric utilities entirely beyond the reach of the States. Other features of this interstate utility business are equally immune from State control either legally or practically."

Thus, in addition to seeking to correct the charging of unreasonable and discriminatory rates in interstate wholesale sales of electric energy which the States were constitutionally powerless to regulate, the act also sought to correct the following practices which were among those disclosed by the Trade Commission's report: Issuance of stocks and other securities on inflated assets; wr te-ups, inadequate depreciation reserves, and other accounting abuses; creation of spheres of influence by mergers of facilities, stock acquisitions, and inter(335)locking directorates; and payment of profits to affiliates out of operating expenses charged to consumers in the rates exacted.

As the Senate committee report said: "Part 2 places the utilities under the regulated conditions which have been prescribed for the principal other national utilities."

Finally, notwithstanding the fact that the unworkable doctrine of *Smythe v. Ames* still held full sway at that time, part II specifically authorized the Commission to ascertain the actual legitimate cost of every public utility, the original cost thereof, the depreciation therein and, when found necessary, other facts, thus carrying forward the regulatory concepts of the 1920 act.

EFFECT ON REGULATION OF RATES AND SERVICE

In exempting practically all sales of electric energy at wholesale in interstate commerce, as well as charges for transmission in interstate commerce, H. R. 2972 would recreate the no man's land in utility regulation which existed before the enactment of the Federal Power Act, resulting from the constitutional inability of the States to regulate such rates. The series of Supreme Court decisions between 1919 and 1927, invalidating repeated State efforts to regulate such rates, as referred to above, was one of the principal factors leading to the enactment of the act (*Public Utilities Commission v. Landon*, 249 U.S. 236 (1919); *Missouri v. Kansas Natural Gas*

Company, 265 U.S. 296 (1924); *Public Utilities Commission of Rhode Island v. Attleboro Steam & Electric Company*, 273 U.S. 83 (1927)).

In the administration of the rate provisions of the Federal Power Act, the Commission has succeeded in establishing the prudent investment principals of rate-making, which has brought with it considerable direct results and probably much greater indirect results in annual reductions in rates to consumers.

The authority, upon request of another electric utility or a State commission, to require an interstate company to interconnect and sell electric energy at wholesale would similarly revert to the no man's land under the proposed amendments. This authority is associated in the act with the congressional purpose to assure an abundant supply of electric energy with the greatest possible economy and with regard to the prober utilization and conservation of natural resources.

The Commission does not believe that the public interest will be served by elimination of the Federal regulation above referred to.

EFFECT ON FINANCIAL REGULATION

In the administration of the act, the Commission, in cooperation with the Securities and Exchange Commission and the States, has been able to render an outstanding service to investors, consumers, and the general public in assuring sound corporate and financial practices.

Notwithstanding the importance of the information and publicity given by the Federal Trade Commission to the existence of write-ups and inflation in the capital structures of electric utilities, aggregating almost one and a half billion dollars, little had actually been done about it before the enactment of the Federal Power Act. Following approval of the act, a national uniform system of accounts based on original cost was promulgated. Capital accounts were required to be

reclassified. Proposed reclassifications, and the underlying cost studies, were examined with care. Where necessary, intensive investigations were made and exhaustive public hearings held. Definitive orders were issued prescribing the accounting reclassifications to be observed and the disposition to be made of write-ups and other excesses over original cost.

As a result, a total of $1,234,186,786 of write-ups and other excesses over original cost has been eliminated or is being eliminated from the accounts of 159 companies under orders issued by the Commission. This amount represents approximately 28 percent of the total reported fixed assets of those companies whose assets in turn represent about 75 percent of the total assets of the 302 companies which have filed reclassification and original cost studies.

Notwithstanding the substantial dollar amounts involved, most of these results have been achieved without formal hearings and without litigation. Where litigation has been necessary the Commission's orders have been sustained. *Northwestern Electric Co. v. Federal Power Commission* (321 U.S. 119); *Pacific Power & Light Co. v. Federal Power Commission* (141 F. (2d) 602); *California-Oregon Power Co. v. Federal Power Commission* (150 F. (2d) 25, certiorari denied, 326 U.S. 781); ef. *American Power & Light Co. v. Securities and Exchange Commis(336)sion* (158 F. (2d) 771 (C.C.A.1), certiorari denied. —U.S.—, No. 1214, October term 1946, decided May 19, 1947). Other companies have not only not opposed the Commission but some have actually gone farther than required by the Commission.

Here again, the Commission's experience indicates that it is against the public interest to permit these gains to be undone or frittered away: or to permit the companies that have not yet disposed of their write-ups and other excesses to avoid doing so; or to permit the former practices to be renewed or old write-ups to be reinstated.

STATE REGULATION

It should be clearly understood that none of these regulatory activities of the Commission interferes with the powers of the States to provide any regulatory requirements or safeguards they may deem necessary. And, of course, regulation of retail rates and local services is left to the States by the present act even where the energy moves in interstate commerce. Where State commissions may be interested in matters pending before the Federal Commission, they are notified and careful provision is made for full consultation and cooperation. State powers of regulation are in no instance weakened by the present act. State power to prescribe accounts required for their regulation of companies subject to their jurisdiction is expressly provided for by the present act, as well as their exclusive power, of regulation of security issues where a company is organized and operating in a State which has a commission regulating security issues.

EFFECTIVENESS OF ADMINISTRATION

Recognition of the value of the Commission's efforts in safeguarding the interests of both investors and consumers has come from those best able to appraise the accomplishment. An example from a representative of the investor viewpoint is found in a recent article appearing in the Wall Street Journal for January 23, 1947, the first of a series of articles on "Utility Operating Companies." The author, 2 years before in the same paper, had said that the Commission's "program of eliminating intangible items and write-ups from the property accounts of many companies" had strengthened "the fundamental position of the electric-utility industry." Now, in commenting upon the current strong financial position of the electric-utility industry, he again gives a predominant emphasis to the accounting adjustments ordered by this Commission in its original cost

proceedings, at the same time recognizing the close relation of those adjustments to the pressure for rate reductions.

An example of the views of consumer representatives is found in a statement by the general counsel of the National Institute of Municipal Law Officers, summing up the effect of the Commission's activities as follows:

"The Commission works in a most difficult field and one which is unspectacular from a publicity viewpoint, but the remarkable results from the Commission's work reveal that taxpayers receive more in tangible returns on their tax dollar for money spend on the Federal Power Commission than for any other Federal regulatory agency" (Rhyne, Charles S., *Municipal Interest in the Work of the Federal Power Commission* (1945) 14 George Washington Law Review 247, 260).

CONCLUSION

H. R. 2972 proposes by indirection to substantially repeal and make utterly unworkable the legislation which has thus so effectively supplemented and strengthened State regulation of electric utilities. This legislation has been a gradual development based on experience, and carefully framed in response to proven needs. Its history shows that it has been supported by both major parties irrespective of any narrow partisan considerations. Its administration has been quiet, but effective.

The administration of this legislation is, of course, not solely responsible for all the gains that have been registered. But neither is its value to be measured solely by the gains that can be seen: the amount of inflation eliminated; the effect of such elimination in accelerating rate reductions throughout the electric utility industry; and the lessening of the corporate and financial abuses formerly so prevalent in the industry. Not the least of the intangible gains are the constant development and improvement of methods of regulation, the training of competent personnel, and the practical demonstration that a

public service of (337) this kind, privately owned and privately managed, can successfully serve the public needs in a manner compatible with the public interest.

We believe that when the facts are understood, your committee will not report favorably this bill which would destroy this important legislation. Before any such report were made, we would respectfully ask for an opportunity to be heard.

The Bureau of the Budget, to whom this report has been submitted in accordance with Budget Circular A-19, advises that there would be no objection to the submission of this report to your committee.

Sincerely yours,

NELSON LEE SMITH, *Chairman.*

FEDERAL POWER COMMISSION REPORT ON H. R. 2973, A BILL TO AMEMD THE FEDERAL POWER ACT

The bill would amend two sections of part I of the act relative to the licensing of hydroelectric projects on streams and lands of the United States. Part I was originally the Federal Water Power Act, approved June 10, 1920, becoming without material change part I of the Federal Power Act by the amendment approved August 26, 1935.

This bill would reverse a national policy with respect to use of water resources that has been maintained for more than half a century. The drastic effect of the proposed amendments will be apparent if the development of this national policy is first briefly traced and the policy explained.

It was not until the close of the last century that the potentialities of central station electric generating plants became apparent. There was an accompanying realization that water power would develop far more energy through an electric generator than it would through the mere production of

mechanical energy to turn a few millstones; and, furthermore, the electric energy so generated could be made available for use in plants located many miles from the water-power plants.

The impetus of this scientific advancement led to expansion of the use of water power as a substitute for fuel. There naturally followed an increase in the pressure for permission to use water-power sites on Government lands and Federal streams. The River and Harbor Acts of 1884 and 1890 had been ineffective in protecting Federal streams and Congress passed the River and Harbor Act of March 3, 1899, which still stands as a bulwark against loss of the public benefits to be obtained from such waters.

The act of 1899 requires Federal approval for obstructions in navigable streams and for interference with lower navigable capacity. In order to provide uniform regulations under which dams across Federal streams could be constructed whenever specifically authorized by Congress, the General Dam Act of 1906 was adopted. These general regulations, however, were materially deficient in several respects, and on April 13, 1908, President Theodore Roosevelt returned to the House of Representatives without his approval a bill which would have granted further time for constructing a power plant in the Rainy River between Minnesota and Canada. In his veto message the President called for a number of special conditions to be incorporated in such authorizations and said: "It should be the duty of some designated official to see that in approving the plans, maximum development of the navigation and power is assured." Although the conditions outlined by the President in this and in his veto message on the James River bill furnished the framework for subsequent legislative policy, there were many long years of debate as to how far that policy should be extended and what public interests it should protect before it became crystallized in the Federal Water Power Act of 1920.

In 1910 Congress passed an amendment to the 1906 General Dam Act, including in the revision many but not all of the conditions mentioned by President Roosevelt. The 1910

revision provided that there should be a comprehensive plan for the development of a river and waterway system; that each project should be given consideration not only with a view to the locality where constructed but with reference to the entire water system of which it constituted a part, and the plans were to be so framed as to bring about the greatest possible development of navigation as well as water power. The acts of 1906 and 1910 were expressly subject to alteration, amendment, or repeal without obligation on the part of the United States, a condition of insecurity not altogether satisfactory to power developers.

APPENDIX O

Excerpts from Supreme Court Brief of Federal Power Commission in *Federal Power Commission v. Florida Power & Light Company*

O-1

In the Supreme Court of the United States

OCTOBER TERM, 1970

No. 958

FEDERAL POWER COMMISSION, PETITIONER

v.

FLORIDA POWER & LIGHT COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

---

* * *

(21)tions were created for facilities used in "local distribution" and facilities used only for the transmission of energy in intrastate commerce or for the transmission of energy consumed wholly by the transmitter (Section 201(b)). Finally, and most important, the Commission's rate jurisdiction over interstate sales was limited to sales at wholesale (*ibid.*); no authority over retail sales was granted.

The question presented in this case is whether FPL's facilities are used for the transmission of electric energy "in interstate commerce" so as to make FPL a "public utility" within the meaning of the Act. It is thus necessary to determine the meaning of the phrase "in interstate commerce."

In the first case to reach this Court under Section 201, *Jersey Central Power & Light Co. v. Federal Power Commission,* 319 U.S. 61, 70-71, a utility seeking to escape the jurisdiction of the Commission argued that the phrase "in interstate commerce" established a very restrictive test of jurisdiction; comparison was made to phrases such as "affecting commerce" of the "current of commerce" used in other regulatory statutes. The Court rejected such comparisons as tools for determining the scope of "interstate commerce," noting that the phrase was precisely defined by the Act itself. 319 U.S. at 70-71. This view of the jurisdictional standard embodied in Section 201 was confirmed by this Court in *Connecticut Light & Power Co. v. Federal Power Commission, supra,* 324 U.S. at 529-531, where it was noted that (22) the "terms of the grant of federal power," as opposed to the terms of limitation employed by Congress to limit jurisdiction, were (324 U.S. at 529):

> ***couched largely in the technical language of the electric art. Federal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test.***

See also *Federal Power Commission v. Southern California Edison Co.*, 376 U.S. 205, 209 n. 5. 215. Thus, the existence or absence of Commission jurisdiction over FPL turns to an analysis of the "engineering and scientific" data contained in the record before the Commission, an analysis the Commission is especially qualified to undertake.

Before turning to the bases for jurisdiction found by the Commission, we reemphasize the significance of this jurisdictional case. As noted, Congress was fully aware of the need for regional planning and coordination of electric systems when it passed the Federal Power Act amendments in 1935. But at that time only a fraction of the nation's systems were interconnected in interstate networks; since that time, interconnection has progressed markedly and the nation's bulk power systems are now being linked from coast to coast. Accordingly, in the words of the Commission "the interstate nature of the electric business, and the need for Federal regulation have steadily risen." Federal Power Commission Report on S. 1365, 90th Cong., (23) printed in Hearings on S. 1365 before the Senate Committee on Commerce, 90th Cong., 1st Sess., p. 5.[14] See also Hearings on H.R. 5348 before Subcommittee on Communications and Power of the House Committee on Interstate and Foreign Commerce, 90th Cong., 1st Sess., p. 118.[15]

The only immediate effect of the Commission's order in this case will be to require FPL to follow the Commission's Uniform

---

[14] S. 1365 was introduced by Senators Holland and Smathers of Florida following the Commission's decision in this case and would have exempted from Commission jurisdiction any utility whose facilities were located entirely within one state and which did not transmit or receive electric energy by direct interconnection from or to any other state or by indirect connection except for temporary or emergency purposes. The bill was never reported out of committee.

[15] H.R. 5348, although differing slightly in language, was the companion bill to S. 1365. See n. 14, *supra*. It too was never reported out of committee.

System of Accounts, thereby subjecting FPL's operations to regulatory and public scrutiny on the same basis as the operations of other utilities. The establishment of jurisdiction over FPL would, however, empower the Commission to order FPL to interconnect with other utilities under certain circumstances, thus improving reliability of service and making possible economies for both parties to the interconnection. See Section 202 of the Act and our brief in *Federal Power Commission v. Florida Power Corp.*, No. 469, 1970 Term, argued February 24, 1971. Commission jurisdiction would also subject FPL's wholesale rates for any future interstate power (24)sales to regulation and FPL would be prohibited from granting undue preference to its wholesale customers as a class or discriminating among them individually (Sections 201(b) and 205). Finally, FPL would also be subject to the provisions of Sections 203 and 204 of the Act, requiring Commission approval of mergers, acquisitions and the issuance of securities, as well as the reporting and other requirements of Part III of the Act, Sections 301-319, 16 U.S.C. 825-825r.

In short, the establishment of jurisdiction in this case will subject one of the nation's largest electric utilities to the specific requirements of the Federal Power Act adopted by Congress to promote the coordinated and efficient deployment of the vast system of interconnected electric facilities which are necessary to meet the nation's power demands. And it will give the Commission the same authority over other similarly situated utilities.

II SUBSTANTIAL EVIDENCE SUPPORTS THE COMMISSION'S DETERMINATION THAT TRANSMISSION OF ELECTRIC ENERGY BETWEEN FPL AND INTERCONNECTED SYSTEMS IN OTHER STATES IS ESTABLISHED BY THEIR ELECTROMAGNETIC UNITY OF RESPONSE

The question whether FPL owns and operates facilities for the transmission of electric energy "in interstate commerce" as that phrase is used and defined in Section 201 of the Federal Power Act, is as we have seen (pp. 21-22, *supra*), a question of "engineering and scientific" fact. The only inquiry on judicial review is to whether the Commission's finding of the existence of that fact was supported by substan(25)tial evidence. See Section 313(b) of the Act; *Federal Power Commission v. Southern California Edison Co.*, 376 U.S. 205, 209 n 5. An analysis of the record shows that there was an abundance of engineering and scientific data to support the Commission's expert conclusion.

As we have set forth in some detail in the Statement (see pp. 7-11, *supra*), the expert evidence introduced before the Commission by the staff established that all of the elements of the interconnected interstate network of which FPL, Corp and Georgia are a part are locked together in electromagnetic unity. Thus, FPL, Corp and Georgia operate in synchronism – *i.e.*, precisely at the same frequency–and the addition of a load or the outage of a generator on one system evokes an almost instantaneous response on the other systems as all generators automatically slow down to provide the additional power necessary to meet the load. The hearing examiner's conclusion that this cause and effect relationship constitutes interstate transmission of electric energy (App. 270) reflects the physical reality of the situation. Clearly, for a generator in one state to alter its mode of operation by reason of the addition of a load in another state, an appropriate signal must be transmitted from the load of the generator. The signal–an electric impulse–is none

other than a quantum of electric energy originating in one state and consumed in another.[16]

(26) The staff evidence, however, was not limited to the bare cause and effect relationship among interconnected facilities, but also concentrated on the degree of coordination of operations among FPL, the other members of the Florida Operating Committee and the other utilities forming the Interconnected Systems Group (see pp. 4-11, *supra*). The substantial interchanges of electric energy among FPL and other Committee members and between Corp and Georgia, the reliance by FPL on other systems for emergency power, and the common use by all ISG members of tie line control with frequency bias to regulate network frequency and to provide almost instantaneous emergency service, all support the conclusion that FPL is an integral part of a vast, coordinated interstate network. This evidence, together with the evidence on the electromagnetic unity of response, fully supports the Commission's conclusion that FPL does, in fact, own facilities for the transmission of electric energy in interstate commerce *i.e.*, in the words of Section 201(c) of the Act, energy "transmitted from a State and consumed at any point outside thereof"

This Court's dictum in *Jersey Central Power & Light Co. v. Federal Power Commission*, 319 U.S. 61, 72, that "[m]ere connection determines nothing" does not compel a rejection of the Commission's determination here. In the first place, the Commission's finding (27) here rested upon much more than the mere fact of FPL's interconnection with an interstate network. But more fundamentally, the Court in *Jersey Central* did not

[16] Compare *Pantomimic Corp. v. Malone*, 238 Fed. 135 (C.C.A.2), where a corporation sought to get around a statute barring the importation of prize fight films by setting up a camera eight inches on the American side of the Canadian border and exposing a banned film eight inches on the Canadian side of the border. The court found the action violative of the customs statute, notwithstanding the fact that only rays of light actually crossed the border.

have before it the evaluation of extensive evidence of the interdependence of interconnected systems that was the basis for the Commission's decision in this case. Although some evidence on the synchronization of interconnected utilities was before the Commission in that case, see 129 F. 2d 183, 187, n. 1, the Commission's order finding Jersey Central to be a "public utility," was based upon express finding that electric energy flows could be traced from Jersey Central over the lines of an intervening utility to the State of New York. 2 F.P.C. 541, 542-543. In view of the limited number of interconnections involved in that case and the relative ease with which the energy flows could be traced, there was no occasion for the Commission or this Court, in affirming the Commission, to consider other bases for jurisdiction. Since Jersey Central, however, several jurisdictional cases have arisen involving situations where the tracing of power flows is not practicable. The decisions of the Commission and courts of appeals in those cases support the Commission's decision here.

In *Indiana & Michigan Electric Co. v. Federal Power Commission*, 365 F. 2d 180 (C.A. 7), certiorari denied, 385 U.S. 972, the Seventh Circuit was faced with the question whether particular sales at wholesale of I & M, an admitted "public utility," involved electric energy in interstate commerce and thus were (28) subject to Commission regulation.[17] In finding all of I & M's sales at wholesale subject to its jurisdiction, the Commission noted that it was impracticable to trace energy flows from specific generating plants to specific loads, but concluded that interstate energy nevertheless pervaded the company's entire system. 365 F. 2d at 182. In upholding the Commission's conclusion, the court of appeals relied on the fact that I & M was part of a coordinated power pool operating as an

[17] Section 201(b) of the Act grants the Commission jurisdiction over "the sale of electric energy at wholesale in interstate commerce." Thus to reach any particular wholesale sale, the Commission must establish as a fact that the sale involves energy "in interstate commerce."

integrated system in several states. This court noted that the "electric load of every customer of every operating company in the System is supplied with electric energy from the entire *** pool" and also discussed at length the dynamics of interconnected power systems and the tie line and frequency control equipment employed by the systems. 365 F. 2d at 182-183. Similar results, based upon analyses of the mode of operation of interconnected utilities forming a power pool where tracing was impractical, were reached by the Sixth and Eighth Circuits in *Cincinnati Gas & Electric Co. v. Federal Power Commission*, 376 F. 2d 506 (C.A. 6), certiorari denied, 389 U.S. 842, and *Arkansas Power & Light Co. v. Federal Power Commission*, 368 F.2d 376 (C.A. 8).[18] (29) Another wholesale rate case, *Public Service Company of Indiana v. Federal Power Commission*, 375 F. 2d 100 (C.A. 7), certiorari denied, 387 U.S. 931, provides an even closer analogy to this case. In contrast to the pooling arrangements of which I & M, Arkansas and

---

[18]The Commission, in *Arkansas Power & Light*, had noted in a passage of considerable relevance here (34 F.P.C. 747, 751, quoted by the court of appeals, 368 F. 2d at 382):

> An interstate electric network is dynamic and ever changing both with respect to load and to generation source. It is an oversimplification, therefore, to talk in terms of a flow of electricity from point to point in an integrated power network of the type involved here. Instead, generation from each source in the system contributes directly or indirectly, and to an ever varying extent, to the energy present, in all parts of the system which are not isolated from out-of-state energy sources. The fact that, as a matter of engineering determination, identification of either the source or destination of particular units of energy within an interstate power system such as respondent's may be difficult and at times impossible does not detract from the interstate nature of the over-all operation. On the contrary, the more complex and comprehensive the nature of the interstate network, the more unlikely it will be that any energy sources will be measurably identifiable. The use of tracing to disprove that a particular sale of a company which is part of an electrically integrated interstate system is in interstate commerce is a wholly unrealistic methodology which is irrelevant to present day power system technology.

Cincinnati were a part, PSCI's relations with its neighbors were far more limited. 34 F.P.C. 1513, 1516-1517. The company was, however, interconnected with six other utilities and, like FPL here, was part of a multi-state, integrated electric power system.[19] In upholding the Commission's as(30)sertion of jurisdiction over PSCI's sales at wholesale, the Seventh Circuit followed the rationale of the *I & M* and *Arkansas* cases and held that the Commission was not required to make specific tracings of power flows. 375 F. 2d-103-104.

The court below sought to distinguish the above case on two grounds: (1) that the utilities there involved were all members of interstate power pools and (2) that establishing wholesale rate jurisdiction over an electric company already subject to Commission jurisdiction is a different matter from establishing jurisdiction over a company in the first instance (App. 369-371). Neither distinction, in our view, is significant.

While undoubtedly FPL's participation in the Florida Operating Committee and the ISG lacks the scope of the pooling arrangements of which I & M, Arkansas, Cincinnati and, to a lesser extent, PSCI were a part, the difference is only one of degree and is not material to the issue whether interstate energy is present in a system or a particular portion of a system.. As we have shown (see pp. 11, 26, *supra*), FPL receives substantial benefits from its participation in the multistate network to which it is electromagnetically locked.

The second attempted distinction is based on the lower court's view that wholesale cases "have little application to the problems of federalism and reservations of power to the states imposed by the instant (31) case, where the issue is one of

---

[19] Referring to the "mere connection" language of this Court in *Jersey Central*, the Commission had noted that "[t]o characterize PSCI's relationships with its neighbors, including those in or receiving power from other states, as mere interconnection is simply to ignore the record." 34 F.P.C. 1513, 1517-1518. Much the same observation can be made with respect to FPL in this case.

whether FPL is a public utility at all ***" (App. 371). As our review of the legislative history of the 1935 amendments to the Federal Power Act indicates, however (see pp. 19-21, *supra*), problems of federalism were very much behind the limitation of Commission rate jurisdiction to sales at wholesale of electric energy in interstate commerce, since the assertion of federal jurisdiction necessarily preempts the jurisdiction of any state authority over such sales. See *Federal Power Commission v. Southern California Edison Co.*, 376 U.S. 205, 210-216. In *Southern California*, this Court referred to the debates in Congress in 1935 concerning the scope of federal wholesale jurisdiction under the proposed amendments and the ultimate decision, based largely on an interpretation of *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 to–

> *** draw a bright line easily ascertained, between state and federal jurisdiction *** making FPC jurisdiction plenary and extending it to all wholesale sales in interstate commerce except those which Congress has made explicitly subject to regulation by the States [376 U.S. 215-216].

Congress employed the same "in interstate commerce" standard to govern Commission jurisdiction over electric utilities as it employed to govern jurisdiction over sales at wholesale; there is no indication in the legislative history that this "bright line" was not to be the same in both situations.

* * *

APPENDIX P

Senate Report No. 621, 74th Congress 1st Session and
House Report No. 1318, 74th Congress 1st Session
(1935)

APPENDIX P.

74th CONGRESS) SENATE Calendar No. 651
1st Session) (REPORT
(No. 621

PUBLIC UTILITY ACT OF 1935

May 13 (calendar day, May 14, 1935.—Ordered to be printed

Mr. Wheeler, from the Committee on Interstate Commerce, submitted the following

REPORT
(To accompany S. 2796)

The Committee on Interstate Commerce, to whom was referred the bill (S. 2796) to provide (in Title I) for the control and elimination of public-utility holding companies operating, or marketing securities, in interstate and foreign commerce and through the mails, and to provide (in Title II) for the regulation of the transmission and sale of electric energy in interstate commerce, for the amendment of the Federal Water Power Act, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass. This bill is a substitute for the bill (S. 1725) introduced on February 6, 1935. In its consideration of the original bill, this committee had before it the printed record of the testimony before the House committee, which heard witnesses upon the companion House bill from February 19 to

April 15, of this year. In addition, page proof of the hearings before this committee, held both mornings and afternoons from April 16 to 29, inclusive, were considered. The proponents of the bill used only 4 days of the hearing time and less than 250 pages of the approximately 1,200-page record. Every objection of the opponents of the bill was carefully considered by the committee in the course of a week of executive sessions, spent in discussing word for ward the original bill and all proposed amendments. As the result of hearings, and the proposed amendments, the committee has so extensively amended S. 1725 that the committee has through it advisable to report a substitute bill.

* * *

(17) holding-company officers and bankers, and the purchase of securities at exorbitant prices from corporate insiders. In short, the individual investor should receive the kind of a security he thought he was buying in the first place. The actual clearing up, through clean reorganizations, of the tangle in which holding-company finance has left the industry and those who have invested in it, can reestablish a confident, stable market for good utility securities. But a frightened policy of refusing to take hold of the obvious political and financial difficulties of the industry will only generate even greater future difficulties.

TITLE II.—CONTROL OF OPERATING UTILITY COMPANIES, AMENDMENTS TO FEDERAL WATER POWER ACT

I. GENERAL PURPOSES OF TITLE II

Title II of the bill repeals two sections and amends certain other sections of the present Federal Water Power Act, and the present act, as this modified, is designated part 1. Two new parts are then added. Part 2 contains substantive provisions for the

regulation of electric energy in interstate commerce. Part 3 contains procedural and administrative provisions applicable to the regulation of licensees under part 1 and interstate public utilities under part 2.

The amendments to the present Federal Water Power Act have been requested by the Federal Power Commission on the basis of its experience in the administration of that act. Most of them are designed merely to clarify the act in its application to situations that have arisen in its administration. The detailed section analysis of the title which follows will make clear the effect of each of these amendments.

In recent years the growth of giant holding companies has been paralleled by the rapid development of the electric industry along lines that transcend State boundaries. To a great extent through the agency of the holding company, local operating units have been tied together into vast interstate systems. As a result the proportion of electric energy that crosses State lines has steadily increased. While in 1928, 10.7 percent of the power generated in the United States was transmitted across State lines, the percentage had increased by 1933 to 17.8. The amount of energy which flowed in interstate commerce in 1933 exceeded the entire amount generated in the country in 1913.

The new part 2 of the Federal Water Power Act would constitute the first assertion of Federal jurisdiction over this major interstate public utility. The decision of the Supreme Court in Public Utilities Commission v. Attleboro Steam & E, Co. (273 U. S. 83), placed the interstate wholesale transactions of the electric utilities entirely beyond the reach of the States. Other features of this interstate utility business are equally immune from State control either legally or practically.

The necessity for Federal leadership in securing planned coordination of the facilities of the industry which alone can produce an abundance of electricity at the lowest possible cost has been clearly revealed in the recent reports of the Federal Power Commission, the Mississippi Valley Committee, and the National Resources Board. Assertion of the power of the

Federal Government in this direction (18) becomes the more important at the time when the Federal Government is compelling the reorganization of holding companies along regional lines. The new part 2 of the Federal Water Power Act seeks to bring about the regional coordination of the operating facilities of the interstate utilities along the same lines within which the financial and managerial control is limited by title 1 of the bill.

Part 2 places the utilities under the regulated conditions which have been prescribed for the principal other national utilities. Commission approval is required before they may issue new securities or consolidate or transfer their operating properties. The Commission is authorized to prescribe the form in which their accounts are to be kept. The sale price of energy sold at wholesale in interstate commerce is made subject to Commission determination.

The Federal Water Power Act, as amended, including the new parts 2 and 3, is given the short title, the "Federal Power Act." This entire act is to be administered by the Federal Power Commission.

2. MATERIAL DIFFERENCES BETWEEN TITLE II OF S. 2795 AND TITLE II OF S. 1725

As has been stated, the committee has liberalized title II of the original bill and endeavored to remove all possible grounds for the charge that is imposes harsh or burdensome restrictions upon the electric industry. The revision has also removed every encroachment upon the authority of the States. The revised bill would impose Federal regulation only over those matters which cannot effectively be controlled by the States. The limitation on the Federal Power Commission's jurisdiction in this regard has been inserted in each section in an effort to prevent the expansion of Federal authority over State matters. In reviewing the material differences between the original bill and the present

one, it will not be necessary to point out all of the places where this jurisdictional limitation has been written into the bill.

A. *Changes in part 1.*—The amendments to the present Federal Water Power Act embodied in part 1 of title II do not differ in any substantial respect from those originally requested by the Federal Power Commission and included in the original bill.

A change has been made in sections 201 and 202 where reference is made to the "actual, legitimate original cost" of a project. These are the words in the present Water Power Act. In S. 1725, the word "prudent" was inserted after "legitimate." The committee has not accepted this amendment. It thinks that the addition of this word is unnecessary and likely to cause confusion. The Federal Power Commission has interpreted the word "legitimate" to give it authority to reject all claims of cost items that are not fair and reasonable charges against the cost of the project. Obviously such an interpretation is the only one which gives effect to the word "legitimate." The committee sees no reason to change the present law under which the Federal Power Commission has effectively exercised the essential power of disallowing imprudent expenditures. To do so might unjustifiably reflect on the past action of the Commission.

An amendment to section 17 of the Water Power Act imposes upon licensees a penalty for delinquency in payment of annual charges. In (19) the original bill this penalty was to be 10 percent of the amount delinquent for the first month and 5 percent for each subsequent month. These figures have been reduced so as to make the penalty 1 percent per month. A moderate penalty should achieve the purpose of securing prompt payment.

Section 212 has been amended to include a repeal of the general penal section of the Federal Water Power Act (sec. 25). The original bill, in part 3, contained a general penalty section applicable to licensees as well as interstate utilities but it did not repeal the present section. This would have left two penal sections in force covering the same offenses.

B. *Assertion of jurisdiction over interstate utilities.*—Section 201 which sets forth the subject matter covered by part 2 of title II has been materially rewritten. A declaration of the necessity for Federal regulation of the interstate part of the electric business has been added as subsection (a). Subsection (b), formerly (a), which states the subject matter to which the part relates, has been clarified to make plain that it includes interstate transmission where there is no sale and excludes all facilities used only for production of transmission in intrastate commerce or in local distribution. A new subsection (e) has been added to remove all doubt that the act is not to apply to public projects, Federal, State of municipal. Despite repeated assurances by representatives of the Federal Power Commission that no such authority was intended, the charge was frequently made that the bill as originally introduced authorized the Commission to compel private utilities to establish connection or exchange power with public plants. This new subsection carries out in unmistakable terms the original intention of the bill in this respect.

C. *Interconnection and coordination of facilities; the common carrier.*—Section 202 (a) of S. 1725 imposed upon each public utility the duty to furnish energy to, exchange energy with and transmit energy for any person upon reasonable request. This provision has been eliminated, and the other subsections of the old section 202 which relate to rates have been removed to the general rate section (sec. 205). While imposition of these duties may ultimately be found to be desirable, the committee does not think that they should be included in this first exercise of Federal power over electric companies. It relies upon the provision for the voluntary coordination of electric facilities in regional districts contained in the new section 202 (a), formerly (formerly sec. 203 (a)), for the first Federal effort in this direction. The authority to compel utilities to establish physical connection with the facilities of other companies and to sell and exchange energy, now contained in section 202 (b), has been limited to cases instituted

by complaint of a State commission or a public utility and to cases in which both parties to the order are interstate utilities. Furthermore, the provisions of the old section 203 (b) empowering the Federal Power Commission to require one utility to permit the use of its facilities by another, or to make extensions or improvements have been eliminated; these matters are left to the voluntary action of the utilities. The emergency powers given the Federal Power Commission which were indefinite in the original bill have been spelled out with particularity in section 202 (c) and appropriately limited to periods of war or other emergency. At such times the Commission may require such temporary connections, and such generation, delivery, (20) interchange or transmission of energy as it considers necessary to meet an emergency shortage.

D. *Certificate of convenience and necessity.*—The requirement in section 204 of S. 1725 that a public utility secure a certificate of convenience and necessity before constructing, acquiring, or abandoning facilities has been eliminated entirely. While it may ultimately be found desirable to adopt a provision of this kind, the committee is of the opinion that for the present there is no imminent danger of excessive extensions that would prove disadvantageous to consumers.

E. *Disposition of facilities.*—Section 203, which was section 205 of the original bill, requires Commission approval of the sale, lease, or other disposition of facilities subject to the act and of the consolidation of such facilities. The section has been changed by eliminating the words "assign", "mortgage", and "encumber" from the sections made subject to approval. As proposed bond issues require approval under the security section, the elimination of these words removes an unnecessary duplication. The section has also been liberalized by limiting its application to facilities of a value exceeding $25,000 and by making it inapplicable to the disposition of property retired from service in the ordinary course of business.

F. *Security issues.*—The security section, now section 204, has been rewritten to attain greater flexibility and workability

than would have been possible under the original section. The language defining the purposes for which securities may be issued has been taken substantially from section 20a of the Interstate Commerce Act, which has proved its usefulness. There has also been added to this section an express provision that preserves the jurisdiction of the State commissions over security issues.

G. *Rates.*—Section 205 (b), transferred from section 202 (e) of the original bill, has been modified by prohibiting merely undue, instead of all, preferences or prejudices in rates. The provisions defining with particularity the power of the Commission to investigate single rates and to fix standards of service (former secs. 208 (b) and 210) and the section authorizing the issuance of reparation orders (former sec. 213) have been eliminated. They are appropriate sections for a State utility law, but the committee does not consider them applicable to one governing merely wholesale transactions. The provision requiring the fixing of rates upon the basis of the actual cost of the property devoted to the service in question (now sec. 208 (c)) has been modified so as to make clear that the rate base is to be no higher than the actual legitimate cost of the property. Furthermore, it is expressly provided that the accrued depreciation of property is to be deducted from the rate base, and the section (302 of S. 1725) requiring the sinking-fund method of depreciation accounting has been eliminated. This practice is contrary to that of most of the States in the country and the committee is of the opinion that its introductic in a Federal statute would cause unnecessary confusion and hardship.

H. *Holding company relations.*—Sections 215 and 216 of the original bill related to service contracts with utilities and the acquisition of utility securities by holding companies. These subjects are fully covered by title 1, and the revised bill removes the duplication.

I. *Accounting.*—In section 301, requiring utilities to keep the accounts prescribed by the Federal Power Commission, a

proviso has been added to make sure that nothing in the act shall relieve any public utility from keeping accounts required by State law.

* * *

74TH CONGRESS) HOUSE OF (REPORT
1st Session) REPRESENTATIVES (No. 1318

PUBLIC UTILITY ACT OF 1935

JUNE 24, 1935.—Committed to the Committee of the Whole House on the state of the Union and ordered to be printed

---

Mr. Rayburn, from the Committee on Interstate and Foreign Commerce, submitted the following

REPORT

[To accompany S. 2796]

The Committee on Interstate and Foreign Commerce, to whom was referred the bill (S. 2796) to provide for the control and elimination of public-utility holding companies operating, or marketing securities, in interstate and foreign commerce and through the mails, to regulate the transmission and sale of electric energy in interstate commerce, to amend the Federal Water Power Act, and for other purposes, having considered the same, report thereon with amendments, and as so amended recommend that the bill do pass.

The first committee amendment strikes out all of the Senate bill and inserts in lieu thereof a substitute which appears in the reported bill in italic type.

The second committee amendment amends the title of the bill to make it conform to the changes made by the committee amendment.

TITLE I. REGULATION OF PUBLIC UTILITY HOLDING COMPANIES

1.THE PRESIDENT'S MESSAGE

On March 12, the President sent the following message to Congress, transmitting a report on public-utility holding companies by the National Power Policy Committee:

To the Congress of the United States:

I am transmitting to you herewith a report submitted to me by the National Power Policy Committee. I named this committee last summer from among the departments of the Government concerned with power problems to make a series of reports to coordinate Government policy on such problems. This report I am submitting to you is the recommendation of the committee with respect to the treatment of holding companies in the public-utility field. It deserves the careful attention of every Member of the Congress.

The so-called "Public Utility Holding Co. bill" (title I of House Bill 3423 and of Senate bill 1725), which was drafted under the direction of congressional leaders incorporates many of the recommendations of this report. * * *

(2)So much has been said through chain letters and circulars and by word of mouth that misrepresents the intent and purpose of a new law that it is important that the people of the country understand once and for all the actual facts of the case. Such a measure will not destroy legitimate business or wholesome and productive investment. It will not destroy a penny of actual value of those operating properties which holding companies now control and which holding-company securities represent insofar as they have any value. On the contrary, it will surround the necessary reorganization of the holding company with safeguards which will in fact protect the investor.

We seek to establish the sound principle that the utility holding company, so long as it is permitted to continue, should

not profit from dealings with subsidiaries and affiliates where there is no semblance of actual bargaining to get the best value and the best price. If a management company is equipped to offer a genuinely economic management service to the smaller operating utility companies it ought not to own stock in the companies it manages, and its fees ought to be reasonable. The holding company should not be permitted to establish a sphere of influence from which independent engineering, construction, and other private enterprise is excluded by a none too benevolent private paternalism. If a management company is controlled by related operating companies, it should be organized on a truly mutual and cooperative basis and should be required to perform its services at actual cost demonstrably lower than the services can be obtained in a free and open market.

We do not seek to prevent the legitimate diversification of investment on operating utility companies by legitimate investment companies. But the holding company in the past has confused the function of control and management with that of investment and in consequence has more frequently than not failed in both functions. Possibly some holding companies may be able to divest themselves of the control of their present subsidiaries and become investment trusts. But an investment company ceases to be an investment company when it embarks into business and management. Investment requires the judicial appraisal of other people's management.

The disappearance at the end of 5 years of those utility holding companies which cannot justify themselves as necessary for the functioning of the operating utility companies of the country is an objective which congressional leaders I have consulted deem essential to a realistic and farsighted treatment of the evils of public-utility companies. For practical reasons we should offer a chance of survival of those holding companies which can prove to the Securities and Exchange Commission that their existence is necessary for the achievement of the public ends which private utility companies are supposed to

serve. For such companies, and during the interim period for other companies, the proposal for a comprehensive plan of public regulation and control is sound.

But where the utility holding company does not perform a demonstrably useful and necessary function in the operating industry and is used simply as a means of financial control, it is idle to talk of the continuation of holding companies on the assumption that regulation can protect the public against them. Regulation has small chance of ultimate success against the kind of concentrated wealth and economic power which holding companies have shown the ability to acquire in the utility field. No Government effort can be expected to carry out effective, continuous, and intricate regulation of the kind of private empires within the Nation which the holding-company device has proved capable of creating.

Except where it is absolutely necessary to the continued functioning of a geographically integrated operating utility system, the utility holding company with its present powers must go. If we could remake our financial history in the light of experience, certainly we would have none of this holding company business. It is only a comparatively late innovation. It dates definitely from the same unfortunate period which marked the beginnings of a host of other laxities in our corporate law which have brought us to our present disgraceful condition of competitive character-mongering between our States. And it offers too well demonstrated temptation to, and facility for, abuse to be tolerated as a recognized business institution. That temptation and that facility are inherent in its very nature. It is a corporate invention which can give a few corporate insiders unwarranted and intolerable powers over other people's money. In its destruction of local control and its substitution of absentee management, it has built up in the public-utility field what has just been called a system of private socialism which is inimical to the welfare of a free people.

Most of us agree that we should take the control and the benefits of the essentially local operating utility industry out of

a few financial centers and give back that control and those benefits to the localities which produce the business and (3) create the wealth. We can properly favor economically independent business, which stands on its own feet and diffuses power and responsibility among the many, and frowns upon those holding companies which, through interlocking directorates and other devices, have given tyrannical power and exclusive opportunity to a favored few. It is time to make an effort to reverse that process of the concentration of power which has made most American citizens, once traditionally independent owners of their own businesses, helplessly dependent for their daily bread upon the favor of a very few, who, by devices such as holding companies, have taken for themselves unwarranted economic power. I am against private socialism of concentrated private power as thoroughly as I am against governmental socialism. The one is equally as dangerous as the other; and destruction of private socialism is utterly essential to avoid governmental socialism.

On April 28, in a radio address to the people of the country, the President supplemented his earlier message on public-utility holding companies as follows:

There is likewise pending before the Congress legislation to provide for the elimination of unnecessary holding companies in the public-utility field.

I consider this legislation a positive recovery measure. Power production in this country is virtually back to the 1929 peak. The operating companies in the gas and electric utility field are by and large in good condition. But under holding-company domination the utility industry has long been hopelessly at war within itself and with public sentiment. By far the greater part of the general management of unnecessary holding-company control has lost touch with and has lost the sympathy of the communities it pretends to serve. Even more significantly, it has given the country as a whole an uneasy

apprehension of overconcentrated economic power in the hands of a very few.

A business that loses the confidence of its customers and the good will of the public cannot long continue to be a good risk for the investor. This legislation will serve the investor by ending the conditions which have caused that lack of confidence and good will. It will put the public-utility operating industry on a sound basis for the future, both in its public relations and in its internal relations.

This legislation will not only in the long run result in providing lower electric and gas rates to the consumer but it will protect the actual value and earning power of properties now owned by thousands of investors who have little protection under the old laws against what used to be called "frenzied finance" and remember that it will not destroy legitimate values.

2.THE GENERAL PURPOSES OF TITLE I

This title seeks to subject to effective public control public-utility holding companies which transcend State lines in their interests and activities. The title seeks to correct the grave abuses disclosed by the reports of the Federal Trade Commission and the reports made for this committee by its special counsel, Dr. Walter M. W. Splawn, now a member of the Interstate Commerce Commission.

Inasmuch as most of the privately owned gas and electric operating companies in the country are controlled by holding companies, the problems involved are many and intricate and of greatest importance, both to the investing and consuming public. The committee gave careful consideration to title I of the Senate bill (S. 1725) which was referred to it, and concluded to report a substitute bill.

The committee substitute contains provisions regulating, under the jurisdiction of the Securities and Exchange Commission, the principal activities of public-utility holding companies and, to the extend deemed necessary, the activities of

their subsidiary companies. These regulatory provisions fall into six fairly well-defined classes as follows:

(1) Issue and sale of securities (secs. 6 and 7);
(2) Acquisition of securities, utility assets, and interests in other businesses (secs. 8, 9, and 10);
(4) (3) Simplification of holding-company systems (sec. 11);
(4) Intercompany transactions (sec. 12);
(5) Service, sales, and construction contracts (sec. 13); and
(6) Reports and accounts (secs. 14 and 15).

The remaining sections of the committee substitute are devoted to such matters as liability for misleading statements (sec. 16), reports of the security transactions of officers and directors (sec. 17), and contain the appropriate provisions for the administration of the title by the Securities and Exchange Commission and its enforcement in the courts.

3. PRINCIPAL DIFFERENCES BETWEEN TITLE I OF THE COMMITTEE SUBSTITUTE AND TITLE I OF THE SENATE BILL (S. 2796)

Title I of the bill as passed by the Senate and title I of the substitute herewith reported are similar in many respects. The section numbers correspond throughout except for the last few sections, and the same subjects of regulation are dealt with. It is not practicable to attempt to set forth all of the differences between the titles of the two bills, but the following statement will indicate the principal differences.

Section 1 (b) has been rewritten so that instead of being in the form of a statement of facts as to abuses which have occurred in connection with the public-utility holding company, it is a statement, based on facts revealed by investigations and hearings, of abuses and conditions the existence or occurrence of which adversely affect the public interest and the interest of investors and consumers. This subsection, by virtue of subsection (c), will furnish a standard for the Commission's

determination of what is in the public interest and the interest of investors or consumers.

Section 2, paragraph 7, in the definition of "holding company" there is omitted the Senate provision under which a company would be a holding company when its ownership of the requisite amount of voting securities of a public-utility company was "in conjunction and pursuant to an arrangement or understanding with one or more other persons."

The definitions of "electric utility company" and "gas utility company" are modified by including therein provisions by which a particular company primarily engaged in one or more other businesses and selling only a small amount of electric energy or gas is to be exempted by the Commission. The House definition of a gas utility company is confined to companies engaged in the retail distribution of gas.

The definition of "affiliate" is restricted so as not to cover so large a number of companies and persons as in the Senate bid.

Throughout the bill where reference is made to a "geographically and economically integrated public-utility system", a phrase which is not defined in the Senate bill, the phrase is changed to "integrated public-utility system" and a definition of it is included.

The defined term "capital assets" is changed to "utility assets".

Section 3 (a) which authorizes the Commission to exempt holding companies and their subsidiaries from the provisions of the title, differs from the provision in the Senate bill. The Senate provision provides that in the case of the exemption of holding companies and (5) their subsidiary companies the exemption shall be from any provision or provisions except insofar as the Commission finds the exemptions from any provision affecting the sale or distribution of securities by any means or instrumentality of interstate commerce detrimental to the protection of investors. The duty of the Commission under the House provision is to make such exemption unless and except insofar as the Commission finds the exemption

detrimental to the public interest or the interests of investors or consumers. Under paragraph (3) of subsection (a), which defines a class of holding companies which may be exempted, the House amendment includes companies not included in the Senate bill, namely, any company which is only incidentally a holding company, being primarily engaged in one or more businesses other than the business of a public-utility company and deriving a material part of its income from one or more subsidiary companies, if substantially all the outstanding securities of such companies are owned directly or indirectly by such holding company.

In section 4 the date prior to which certain holding companies are required to register if they are to carry on their interstate activities is changed from October 1 to November 1, 1935; and there is omitted paragraph (6), under which it would be unlawful for an unregistered holding company to own, hold, or control any security of any subsidiary company thereof that does any of the acts enumerated in the five preceding paragraphs. Corresponding changes are made in the dates in subsection (b).

Section 5 is changed in striking out certain paragraphs in subsection (b), providing for the filing of information after registration.

Sections 6 and 7 relating to Commission approval of the issuance of securities and the changing of priorities, preferences, voting power, and other rights of holders of outstanding securities are modified so that the only subsidiary companies subject thereto are public utilities the issuance of whose securities is not subject to regulation by a State commission.

Section 6 is modified by striking out subsection (c) relating to house-to-house sales of securities and substituting a provision making it unlawful for any registered holding company to cause employees of a subsidiary company to sell the securities of the holding company.

Section 7 is amended by striking out subsection (f), relating to the prescribing of terms and conditions by the Commission in

connection with permitting a declaration regarding the issuance of securities to become effective; subsection (g), relating to the requirement that a declaration should not become effective unless applicable State laws shall have been complied with; and subsection (h), a provision intended to bring about prompt registration by companies expecting to issue securities.

Sections 8, 9, and 10 are modified so that the requirement that a registered holding company of subsidiary company should not acquire any interest in any business other than (1) a public-utility company as such, or (2) a business in which the acquiring company is already engaged or has an interest, or which is reasonably incidental or necessary or appropriate to the conduct of such business, is omitted. There is also omitted the provision which prohibited acquisitions bringing into holding-company systems natural-gas properties or pipe lines. These sections are also modified so as to require Commission (6) approval not only of securities and utility assets as under the Senate bill, but also of the acquisition of any other interest in any business. The provision that no acquisition of securities or utility assets is to be approved unless State laws are complies with is extended to cover the acquisition of any other interest, but the whole provision is conditioned by providing that the provision shall not apply where it would be detrimental to carrying out the provisions of section 11.

Section 11, relating to the simplification of holding-company systems and the elimination of holding companies, is modified so that the only remaining provision providing for simplification or elimination makes it the duty of the Commission to require each holding-company system to confine its operations to one integrated public-utility system, with the exception that if the Commission finds that such a limitation is not necessary in the public interest, it is to require the limitation of the operations of the holding-company system to such number of integrated public-utility systems as it finds may be included in the holding-company system consistently with the public interest. The Commission is authorized to require divestment of

nonutility property only where it finds the retention thereof would be inconsistent with the public interest, and the Commission is further limited in that it may not require divestment of interests outside of the United States. The Commission may proceed either upon its own motion or upon application of the companies involved, but may proceed upon its own motion only after January 1, 1938. The provisions relating to special judicial procedures in connection with divestment are eliminated from section 11, and the orders of the Commission are to be enforced in the same manner as its other orders issued under the title.

Section 12 is amended by striking out subsection (g), relating to a prohibition upon affiliates of public-utility companies or registered holding companies or subsidiary companies thereof entering into transactions with the companies of which they are affiliates, in contravention of the regulations of the Commission.

Section 13, relating to service, sales, and construction contracts is modified in several material respects. The provisions for setting up mutual service companies are eliminated, the absolute restriction on subsidiary companies entering into or performing service, sales, or construction contracts with public-utility companies in the same holding-company system is eliminated, and a new provision is included which makes it unlawful for any subsidiary of the registered holding company to enter into or perform any service, sales, or construction contracts with other companies in the same holding-company system in contravention of the rules, regulations, or orders of the Commission. The provision relating to the performance of these contracts by affiliates has been eliminated.

Section 15 is amended by striking out subsection (e), giving authority to the Commission to prescribe uniform methods of accounts for persons subject to subsection (a) and (b) of this section, and subsection (j) is omitted for the reason that it was considered to be unnecessary.

Section 17 (a) and (b), referring to reports by officers, directors, and affiliates, and giving a remedy in the case of

unfair use of information by officers, directors, or affiliates are changed by striking out the reference to affiliates and by providing that the section shall not give a remedy where one is given under section 16 (b) of the Securities Exchange Act of 1934.

(7) Section 21 is changed by omitting the sentence providing that "Nothing in this title shall exempt any public-utility company from obedience to the law of any State in which it operates", on the theory that it imposed a limitation which might interfere with the carrying out of the provisions of section 11 or other sections, under which it might be necessary to do things not permitted under State law.

Section 25 is changed so as to give State courts concurrent jurisdiction with the Federal courts of suits in equity and actions at law brought to enforce any liability or duty created by, or enjoin any violation of the title or the rules, regulations, or orders thereunder.

The penalty provision (sec. 29) is modified so that the fine of not more than $200,000 which may be imposed in case of failure of a holding company to register as required, will only apply were the holding company is not an individual. The maximum fine applicable to an individual is $10,000.

Section 30, providing for an investigation of public-utility companies in order to determine the size and type most appropriate to serve the public interest and providing for a study of investment trusts and companies, is omitted as surplusage.

Under the Senate bill the Federal Power Commission was vested with certain functions under title I. Under the committee substitute all such functions are vested in the Securities and Exchange Commission.

TITLE II. AMENDMENTS TO FEDERAL WATER POWER ACT; REGULATION OF INTERSTATE ELECTRIC UTILITY COMPANIES

GENERAL PURPOSES OF TITLE II

Title II of the bill makes certain amendments to the present Federal Water Power Act and establishes for the first time regulation of electric utility companies transmitting energy in interstate commerce. The amendments to the Water Power Act appear at the beginning of the title. The present Water Power Act is made part I of the amended Federal Power Act. Two new parts are then added: Part II consisting of the substantive provisions for the regulation of interstate operating companies; and Part III containing the general provisions applicable to both licenses under part I, and interstate utilities under part II.

The amendments to the present Federal Water Power Act are all minor. They have been requested by the Federal Power Commission, largely for the purpose of clarifying the act in its application to situations that have arisen in its administration, and also to strengthen it in certain particulars. The effect of these amendments is shown in the detailed section analysis which follows.

The new parts are designed to meet the situation which has been created by the recent rapid growth of electric utilities along interstate lines. The percentage of electric energy generated in the United States that was transmitted across State lines increased from 10.7 in 1928 to 17.8 in 1933. The amount of energy transmitted in interstate commerce in 1933 was greater than all of the energy generated in the country in 1913. Under the decision of the Supreme Court of the United Stated in Public Utilities Commission v. Attleboro Steam & E. Co. (273 U. S. 83), the rates charged in interstate wholesale (8) transactions may not be regulated by the States. Part II gives the Federal Power Commission jurisdiction to regulate these rates. A "wholesale" transaction is defined to mean the sale of electric

energy for resale and he Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce.

Part II gives control over security issues of interstate operating companies in cases where no State commission has control and over the consolidation, purchase, and sale of interstate operating properties. The bill also provides for the establishment of regional districts for the interconnection and coordination of electric facilities by the voluntary action of the utilities within and between the districts. Whenever such voluntary measures are found to be ineffective, the Commission is given limited authority, upon complaint of a State commission or an operating utility, to require physical connection and the sale of interchange of energy. The bill also authorizes the Commission to ascertain the cost of property used in rendering service; to prescribe a uniform system of accounts; to determine proper depreciation rates and to make investigations and reports to Congress relating to the electrical industry.

The bill takes no authority from State commissions and contains provisions authorizing the Federal Commission to aid the State commissions in their efforts to ascertain and fix reasonable charges. Provision is made for joint boards composed of members of State commissions which may be used for this purpose. The new parts are so drawn as to be a complement to and in no sense a usurpation of State regulatory authority and contain throughout directions to the Federal Power Commission to receive and consider the views of State commissions. Probably, no bill in recent years has so recognized the responsibilities of State regulatory commissions as does title II of this bill.

SECTIONAL ANALYSIS OF BILL

TITLE I

SECTION 1. BASIS OF JURISDICTION AND NECESSITY FOR REGULATION OF PUBLIC-UTILITY HOLDING COMPANIES

Subsection (a) sets forth the facts by reason of which public-utility holding companies are affected with a national public interest.

Subsection (b) contains an enumeration of the conditions which justify Federal regulation of public-utility holding companies in the national public interest.

Subsection (c) declares the legislative policy embodied in title I to be that of meeting the problems and eliminating the abuses connected with public-utility holding company systems.

SECTION 2. DEFINITIONS

Subsection (a) contains definitions of 27 terms that are used throughout the title, such as security, holding company, subsidiary company, associate company, affiliate, integrated public-utility system, service contract, sales contract, construction contract, utility assets, and others. Most of the definitions are self-explanatory and mention is here made only of the more important of these definitions.

(9) "Commission" (6) is defined as the Securities and Exchange Commission, and the administration of the title is vested in that Commission.

"Electric utility company" (3) is defined to include both wholesale and retail sellers of electric energy, and transmission companies, with appropriate exemptions by order of the Commission, upon application, for companies which are primarily engaged in businesses other than the business of an electric utility company.

"Gas utility company" (4) includes only those companies which distribute natural or manufactured gas at retail or own facilities for such retail distribution, with appropriate exemptions by order of the Commission, upon application, for companies that are primarily engaged in businesses other than the business of a gas utility company.

"Holding company" (7) is defined in two parts: (A) In terms of owning or controlling, directly or indirectly, 10 percent or more of the voting securities of a utility (gas or electric) company or another holding company, or of holding such securities with power to vote; and (B) in terms of "exercising a controlling influence" over the management or policies of a utility company. Under the flexible definition in (B), no company is to be deemed a holding company or have any duty as such until the Commission so finds after notice and opportunity for hearing. The flexibility here provided is necessary in order that title I can meet the varied and subtle forms which corporate interrelationships have in the past and will in the future take. A company which is automatically a holding company under (A) by reason of stock ownership, control, or holdings, can nevertheless file an application for determination that it is not a holding company in terms of controlling a public-utility company. Pending the Commissions' action on such an application, the provisions of the title are suspended as to the applicant. The denial of an application does not, of course, preclude a company from making another application after a change of circumstances.

"Subsidiary company" (8) is also defined, conversely from "holding company", in terms of stock ownership or control, or in terms of holding stock with power to vote, and subsection to a controlling influence; the same administrative machinery for Commission determination and exemption is provided.

"Holding company system" (9) is used to designate a holding company and all its subsidiary companies.

"Associate company" (10) of a company is used to designate any other company in the same holding company system with such company.

"Affiliate" (11) is a term which includes some of the common relationships which make for an absence of arms'-length bargaining. The definition, like that of "holding company", embraces two parts: The first two clauses are of automatic application. The first defines as affiliates companies with a certain relation by stock ownership or control, or by holding stock with power to vote. The second makes the officers and directors of a company affiliates of that company. The third clause is the flexible provision which operates only after the Commission determines that the person or company involved stands in such relation to another company that there is such an absence of arm's-length bargaining in the transactions between them as to make it necessary or appropriate in the public interest that such (10) person or company be subject to the obligations, duties, and liabilities imposed in title I upon affiliates. Again in the flexible clause ample protection is given by providing in subsection (b) of this section that no person shall be deemed an affiliate under the flexible clause until after the Commission has made its determination and notified the party affected.

"Utility assets" (16) is defined to include only the facilities, in place, of an electric or gas utility company.

"Voting security" (17) is defined, in part, to mean a security presently entitling the owner or holder to certain voting rights. Some securities are issued with the privilege of voting only under specific circumstances and the purpose of using the word "presently" is to refer to securities as of the time when the security carries the privilege of voting.

"Integrated public-utility system" (27) is defined to mean—(A) as applied to electric utility companies, a system consisting of one or more units of generating plants and/or transmission lines and distributing facilities, whose utility assets, whether owned by one or more electric utility companies,

are physically interconnected or capable of physical interconnection and which under normal conditions may be economically operated as a single interconnected and coordinated system confined in its operations to a single area or region, in one or more States, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management and efficient operation: and (B) as applied to gas utility companies, a system consisting of one or more gas utility companies which are so located and related that substantial economies may be effectuated by being operated as a single coordinated system confined in its operations to a single area or region, in one or more States, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management and efficient operation, provided that gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region.

Subsection (b) gives the necessary protection to the persons and companies which will become holding companies, subsidiary companies, or affiliates under the flexible provisions of those definitions by providing that they shall not be deemed to be such until 30 days after the Commission's determination on a hearing.

Subsection (c) states that no provision of the title shall apply to the United States or any State or political subdivision thereof or to any agency of any of the foregoing unless specific reference is made thereto.

SECTION 3. PARTICULAR EXEMPTIONS REGARDING HOLDING COMPANIES, SUBSIDIARY COMPANIES, AND AFFILIATES

Subsection (a) describes five classes of companies which, although technically holding companies under the definitions, are essentially not the kind of public-utility holding companies at which the purposes of the legislation are directed, for one of

the following reasons: (1) The whole system is intrastate; (2) the company is itself a utility, being a holding company only in form by reason of the fact that it has one or more minor subsidiary utilities; (3) the company is not (11) essentially in the utility field and either (A) gets no appreciable income from utilities, or (B) if it gets an appreciable income from utilities, it owns all the outstanding securities of those utilities so that they are not financed by the public but are essentially departments, rather than subsidiaries, of the parent company; (4) the company is temporarily a holding company solely by reason of the acquisition of securities for purposes of liquidation of a bona fide debt, or in connection with a bona fide arrangement to underwrite the securities; or (5) the company has no subsidiary utilities in the United States and is not itself a domestic utility.

It is the duty of the Commission, as to any company which it finds to fall in one of these five categories, to exempt such company from any provision or provisions of title I to the extent it deems such exemption not detrimental to the public interest or the interest of investors or consumers. By thus imposing a mandatory duty upon the Commission to exempt companies falling within defined categories except where such exemption is definitely detrimental to the basic purposes of the statute, the committee has felt free to broaden the exemptions beyond what would be justified if the exemptions had been made unqualified and self-operative and beyond the power of the Commission to correct when abused or used to circumvent the purposes of the title. On the other hand, companies entitled to exemption from this subsection as holding companies or as subsidiaries of exempted holding companies may still be subject to the provisions of title I as subsidiaries of other holding companies which are not exempted, unless they are exempted by reason of subsection (b) or some other provision of the title.

Subsection (b) authorizes the Commission to exempt specified classes of affiliates or subsidiary companies from one or more provisions of the title if and to the extent the Commission deems such exemption necessary or appropriate in

the public interest or for the protection of investors or consumers.

SECTION 4. TRANSACTIONS BY UNREGISTERED HOLDING COMPANIES

This section establishes the mechanism by which holding companies are brought under the jurisdiction of the Commission so that the provisions of title I may be effectively administered. That mechanism is registration, and it is made the duty of every holding company, unless exempted, to register by November 1, 1935, if it is to carry on any of the activities which are national in scope and hence of particular concern to the Federal Government. Unregistered companies after that date are prohibited from engaging in these activities unless they are registered.

Subsection (a) enumerates the acts involved as follows:

(1) To sell, transport, or transmit gas or electric energy in interstate commerce or to own or operate any capital assets for so doing.

(2) To use the mails or any means or instrumentalities of interstate commerce for the performance of any service, sales or construction contract for a public-utility or holding company.

(3) To use the mails or means or instrumentalities of interstate commerce to distribute or make a public offering of any security of the company, any of its subsidiary companies or affiliates, or any public-utility or holding company, or to sell any such security to any

* * *

APPENDIX Q

Glossary of Terms

ATTACHMENT A

GLOSSARY[1]

BULK ELECTRIC SYSTEM

A term commonly applied to the portion of an electric utility system that encompasses the electricl generation resources and bulk transmission facilities.

COMPETITIVE ACCESS

Access by suppliers of electricity to transmission grids, leading to competition with owners of such grids and other suppliers.

GENERATION (Electricity)

The process of producing electrical energy from other forms of energy; also, the amount of electric energy produced, usually expressed in kilowatthours (kWh) or megawatthours (MWh).

Generation, **Gross**

The electrical output at the terminals of the generator, usually expressed in megawatts (MW).

Generation, **Net**

Gross generation minus station service or unit service power requirements, usually expressed in megawatts (MW).

---

[1] Selected and adapted from the Glossary of Terms prepared by the Glossary of Terms Task Force of the North American Electric Reliability Council.

LOCAL DISTRIBUTION FACILITIES

The facilities that bring electricity from the transmission system to end users.

MUNICIPALIZATION

The process by which a new municipal utility is formed to serve former retail customers of a utility. The new municipality will purchase electricity at wholesale for the benefit of its residents.

REGULATION

The setting of rates, terms and conditions for a particular service, the establishment of standards for the safety and reliability of the service and the handling of customer complaints.

RETAIL CONSUMER

A customer taking electric service for its own use; an end user.

RETAIL STRANDED COSTS

Costs that a utility incurred to serve end-users and that cannot be recovered because the customers are lost as a result of competitive access to other utility systems. The term "stranded costs," in a general sense, refers to the difference between the net embedded costs of utility plant and the plant's market value. It can also encompass factors such as transaction costs associated with reducing a company's work force, carrying charges on excess capacity or revenue losses due to customer migration to competitive alternatives. These

stranded costs will be associated, for the most part, with generation plant, since the competition will be for generation.

REVENUE REQUIREMENT

The capital costs and expenses that a company normally recovers through regulated rates.

RETAIL TRANSMISSION SERVICE

Transmission provided to a retail customer.

TRANSMISSION

An interconnected group of lines and associated equipment for the movement or transfer of electric energy between points of supply and points at which it is transformed for delivery to distribution systems or is delivered to other electric systems.

UNBUNDLING

The separation of the businesses of transporting electricity and selling the energy previously combined in a "bundled" rate into two rates, one for transport and one for energy.

WHOLESALE DISTRIBUTION SERVICE

Use of the local distribution service to deliver electricity to a wholesale customer (who intends to resell to an end user).

WHOLESALE SALE

A sale of electric energy to an entity that intends to sell it for resale.

Q-4

WHOLESALE TRANSMISSION SERVICE

Transmission provided to a wholesale customer (who intends to use the transmission to resell electricity to an end-user).

APPENDIX R

List of Parties

LIST OF PARTIES

Pursuant to Rule 14 of the Supreme Court of the United States, the petitioners and intervenors before the Court below are as follows:

Action Alliance of Senior Citizens of Greater Pennsylvania

Alabama Power Company, et al.
(The Southern Companies)

American Public Power Association

American Forest & Paper Association

American Iron And Steel Institute

Arkansas Public Service Commission

Atlantic City Electric Company

Board of Water, Light And Sinking Fund
Comm'ns of City of Dalton, Georgia

Boston Edison Company, et al.

Cajun Electric Power Coop. Inc. (Trustee)

Carolina Power & Light Company

Central Montana Electric Power Cooperative, Inc.

Central Vermont Public Service Corporation

Chemical Manufacturers Association

Cincinnati Gas & Electric Co.

Citizens For a Sound Economy

Citizens Power, Inc.

Citizens Action Coalition of Indiana, Inc.

Cities of Benton, et al.

The City and County of San Francisco

City of Alma, Michigan

City of Cleveland, Ohio

City of Lakeland, Florida

City of Tallahassee, Florida

Coalition For Economic Competition

Commonwealth Edison Company

Consolidated Edison Company of New York, Inc.

Consumer Energy Company

Council of Industrial Boiler Owners

CSW Operating Companies
(Central Power & Light Company, West Texas Utilities Company, Public Service Company of Oklahoma and Southwestern Electric Power Company)

Dairyland Power Cooperative

The Dayton Power and Light Co.

The Detroit Edison Company

Duke Energy Trading And Marketing
(Formerly PANENERGY Trading and Market Services)

Edison Electric Institute

Electric Clearinghouse, Inc.

Electricity Consumers Resource Council

Electric Power Supply Association

El Paso Electric Company

ENRON Power Marketing

ENTERGY Services Inc.

Federal Energy Regulatory Commission

First Energy Corp.
(Formerly Ohio Edison Company, The Cleveland Electric Illuminating Co., and The Toledo Edison Co.)

Florida Municipal Power Agency

Florida Power Corporation

Florida Power & Light Company

Florida Public Service Commission

Gainesville Regional Utilities

Georgia Transmission Corporation

GPU Energy Companies
(Formerly, General Public Utilities Service, Inc.)

H.Q. Energy Services (U.S.)

Hydro-Quebec

Idaho Public Utilities Commission

Illinois Commerce Commission

Illinois Power Company

Indiana Industrial Energy Consumers, Inc.

Indiana Office of Utility Consumer Counselor

Indianapolis Power & Light Co.

Jacksonville Electric Authority

Kansas City Power & Light Company

Kissimmee Utility Authority

Long Island Lighting Co.

Louisiana Energy And Power Authority

Massachusetts Municipal Wholesale Electric Company

Michigan South Central Power Agency

Multiple Intervenors

Municipal Electric Utilities of Wisconsin

National Association of State Utility Consumer Advocates

National Rural Electric Cooperative Association

National Association of Regulatory Utility Commissioners

Nebraska Public Power District

New England Electric Service

New England Power Company

New Jersey Board of Public Utilities

New York State Electric & Gas Corporation

Niagara Mohawk Power Corp.

North Carolina Utilities

Commission And The Public Staff of The North Carolina Utilities Comm'n

Northeast Texas Electric Cooperative of Texas, Inc.

Northeast Utilities Service Company And Northeast Utilities

Ohio Consumers' Counsel

Ontario Hydro

PANENERGY Trading and Market Services

Pennsylvania Consumer Action Network

Pennsylvania Municipal Electric Association

Pennsylvania Rural Electric Association, et al.

People of The State of New York, et al. and Public Service Commission of The State of New York

PSI Energy, Inc.

Public Citizen, Inc.

Public Power Association of New Jersey

Public Service Company of New Mexico

Public Service Electric & Gas Company

Public Utilities Commission of The State of Colorado

Puget Sound Energy, Inc.

Rochester Gas & Electric Corporation

Safe Energy Communication Council

Sam Rayburn G&T Electric

San Diego Gas & Electric Co.

SASKPOWER

Southern California Edison Co.

South Carolina Electric & Gas Company

Southern California Gas Company

Suffolk County Electrical Agency

Tex-La Electric Cooperative of Texas, Inc.

Transmission Access Policy Study Group

Transmission Dependent Utility Systems

United Homeowners Association

U.S. Public Interest Research Group

Vermont Department of Public Service

Virginia Electric & Power Co.

Virginia State Corporation Commission

Washington Utilities and Transportation Commission

Wisconsin Power & Light Co.

Wisconsin Public Service Corp.

Wolverine Power Supply Cooperative, Inc.

Wyoming Public Service Commission

Supreme Court, U.S.
FILED
JAN 26 2001
OFFICE OF THE CLERK

(3) (2) (4)

Nos. 00-568, 00-800, and 00-809

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

---

BRIEF OF RESPONDENT TRANSMISSION ACCESS POLICY STUDY GROUP

ROBERT C. MCDIARMID
Counsel of Record
CYNTHIA S. BOGORAD
BEN FINKELSTEIN
PETER J. HOPKINS
SPIEGEL & MCDIARMID
1350 New York Ave., NW
Suite 1100
Washington, DC 20005
(202) 879-4000

January 26, 2000

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

TABLE OF CONTENTS

TABLE OF AUTHORITIES..... i
ARGUMENT 1
REASONS WHY THE STATES' PETITION SHOULD BE DENIED..... 2
I. PETITIONER'S FIRST POINT RESTS UPON A PREMISE REJECTED BY THIS COURT AND CONTRARY TO THE RECORD BELOW, AND SEEKS REVIEW OF AN ALTERNATIVE (AND SOUND) HOLDING..... 2
II. THE STATES' SECOND POINT RESTS UPON THE INVALID PREMISE THAT THE STATES CAN REGULATE WHOLESALE ELECTRIC POWER SALES 4
CONCLUSION 6

TABLE OF AUTHORITIES

Cases:

Arkansas Power & Light Co. v. FPC, 368 F.2d 376 (8th Cir. 1966) 5
Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) 5
Duke Power Co. v. FPC, 401 F.2d 930 (D.C. Cir. 1968).....6
FPC v. Florida Power & Light Co., 404 U.S. 453 (1972) 2,3,4
FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) 4
Florida Power & Light Co., 37 F.P.C. 544 (1967), *aff'd*, 404 U.S. 453 (1972).....3
Hillsborough County v. Automated Medical Labs, Inc., 471 U.S. 707 (1985) 4
Massachusetts v. Morash, 490 U.S. 107 (1989).....4

Mississippi Power & Light Co. v. Mississippi ex rel. Moore, 487 U.S. 354 (1988) 4
Northern States Power Co. v. FERC, 176 F.3d 1090 (8th Cir. 1999), *cert denied*, 120 S. Ct. 1221 (U.S. 2000) 4
Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) 1
Public Utilities Comm'n v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927) 5
Wisconsin-Michigan Power Co. v. FPC, 197 F.2d 472 (7th Cir.1952) 6

Statutes:
Federal Power Act, 16 U.S.C. §§ 792 *et seq.*
16 U.S.C. § 824(a) 2,4
16 U.S.C. § 824(b)(1) 4

ARGUMENT

Respondent Transmission Access Policy Study Group ("TAPS")[1] respectfully requests that this Court deny the petitions of the States and Dalton for writ of certiorari, seeking review of the District of Columbia Circuit's opinion. Because Dalton's petition is without merit and warrants little discussion,[2] TAPS addresses only the States' petition below.[3] TAPS believes that Petitioner Enron Power Marketing, Inc.'s position is correct, but because under the D.C. Circuit's opinion the Federal Energy Regulatory Commission ("FERC") may choose to exercise jurisdiction in the future over all interstate transmission by public utilities, including transmission used for "bundled" [4] retail electric sales, there is no need for the Court to review the issue now. However, should the Court grant States' petition then it should also grant Enron's petition to permit a complete assessment of the issues.

The opinion is reported at 225 F.3d 667, *amended*, 2000 U.S. App. LEXIS 15362 (D.C. Cir. Nov. 14, 2000).

---

[1] TAPS is an informal association of municipal, cooperative and investor-owned utilities and other supporters in more than 29 states, promoting open and non-discriminatory transmission access. Many TAPS members are entirely or predominantly transmission-dependent. States Pet. App. C-29. Unless otherwise noted or obvious all references herein are to States' Petition and Appendices.

[2] Contrary to Dalton's claim (Pet. 8), FERC based its order on a generic finding of *existing* undue discrimination in transmission services. *See* Enron Pet. App. D-192a, 213a, E-437a. Also, Dalton (Pet. 24) misreads *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973), as barring FERC from ordering transmission service to cure undue discrimination, a matter not reached in the Court's decision.

[3] TAPS responds to questions 1, 2 and 4 of the States' Petition.

[4] In a bundled retail sale transmission and electric energy are provided and sold together under one rate, and in an unbundled sale they are provided and sold separately. Pet. App. Q-3.

REASONS WHY THE STATES' PETITION SHOULD BE DENIED

I. PETITIONERS' FIRST POINT RESTS UPON A PREMISE REJECTED BY THIS COURT AND CONTRARY TO THE RECORD BELOW, AND SEEKS REVIEW OF AN ALTERNATIVE (AND SOUND) HOLDING

Petitioners States challenge the decision below because it affirms FERC's regulation of transmission used for unbundled retail electric sales, arguing that this is an impermissible regulation of "the transmission of electricity from a generator to a retail customer in the same state ...." Pet. 10. Their objection rests upon the discredited premise that a modern electric system directly transmits electrons "from a generator to a retail customer." *Id.* This is not how an integrated and interconnected electric transmission system works. The precedent of this Court and the decision and order below correctly find that power on an integrated and interconnected electric system "comes from a variety of sources" and is "commingled just as molecules of water from different sources (rains, streams, etc.) [are] commingled in a reservoir." *FPC v. Florida Power & Light Co.*, 404 U.S. 453, 461 (1972). This commingled power is energy transmitted "in interstate commerce" within the meaning of the Federal Power Act ("FPA") and thus transmission subject to FERC's jurisdiction.

The FPA authorizes FERC to regulate "the transmission of electric energy in interstate commerce." FPA § 201(a), 16 U.S.C. § 824(a) (1994). Based upon this language, as construed by this Court, the D.C. Circuit affirmed FERC's jurisdiction over the transmission component of unbundled retail sales. The decision properly found this Court to have held that FERC had plenary jurisdiction over the

transmission by nearly[5] "every privately owned interconnected [utility] in the United States ...." Pet. App. C-33 (quoting *FP&L*, 404 U.S. at 471 [Douglas, J., dissenting]).[6] *FP&L* is consistent with FERC's expert determination below: transmission used to support unbundled retail sales, like all transmission, is transmission of a commingled stream of electrons from multiple, including interstate, sources.[7] "Because of the highly integrated nature of the electric system, ... most transmission of electric energy [is] 'in interstate commerce.'" Pet. App. D-90.

There is no support in the decision or orders below (or otherwise) for the States' contention that there is direct transmission of electricity from a generator to a retail customer in the same state. At best, the States' jurisdictional challenge rests upon a fictional "contract path for a particular power or transmission sale ...." Pet. App. D-90. But as the decision and order below correctly recognize, this Court has held that federal jurisdiction follows the "engineering and scientific" flow of electricity, not fiction. Pet. App. D-91; *see also* Pet. App. C-31–33 (same).

Contrary to States' fourth question (Pet. i), the D.C. Circuit did not improperly defer to FERC's interpretation of its

---

[5] There is intrastate transmission in Alaska, Hawaii and (arguably) portions of Texas because electric utility systems in these states are not interconnected (or interconnected only through direct current ties) with electric systems in other states. The States concede that FERC is not seeking to exercise jurisdiction over such transmission. Pet. 16 n.10. *See also* Pet. App. D-43 n. 541.

[6] The decision below strongly suggests that FERC could exercise jurisdiction over the transmission component of bundled retail electric sales, but as "a statutorily permissible policy choice" declined to do so. Pet. App. C-34.

[7] Contrary to States' assertion (Pet. 12), *FP&L* did involve federal preemption of state regulation. *FP&L* affirmed the Federal Power Commission's ("FPC") finding that Florida Power "must comply with all ... requirements of the Commission's Regulations under the [FPA]." *Florida Power & Light Co.*, 37 F.P.C. 544, 546 (1967), *aff'd*, 404 U.S. 453 (1972).

jurisdiction. As the States concede (Pet. 7), deference is an alternative holding reached only after the decision affirmed FERC's jurisdiction based on this Court's precedent construing the FPA. This alternative holding does not raise a question worthy of certiorari.

In any event, such deference is consistent with numerous decisions of this Court. *See, e.g.*, *Massachusetts v. Morash*, 490 U.S. 107, 116-118 (1989); *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354, 380-81 (1988) (and cases cited therein). Seeking to rely upon *Hillsborough County v. Automated Medical Labs, Inc.*, 471 U.S. 707, 715 (1985), a decision not involving the FPA, the States argue that it is wrong to defer to FERC's interpretation of its jurisdiction because the FPA reserves certain powers to the states. However, in *MP&L*, decided subsequent to *Hillsborough*, Justice Scalia, writing in concurrence, explained that the *MP&L* Court did just that, *i.e.*, deferred to FERC's assertion of jurisdiction over purportedly state matters. *MP&L*, 487 U.S. at 380-81. Similarly, in *FP&L*, 404 U.S. at 463, the Court deferred to the FPC's "technical expertise and experience" in affirming federal jurisdiction over matters allegedly left to the states.

It is not clear there is a conflict between the decision below and *Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999), *cert. denied*, 120 S. Ct. 1221 (U.S. 2000). *NSP*, 176 F.3d at 1096, held only that FERC had "no jurisdiction ... over the state's regulation of NSP's bundled retail sales activities," based upon FERC's own jurisdictional "conce[ssion]." If States' reading of *NSP* were correct, that decision would be in conflict with the holding in *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972), that under the Natural Gas Act the FPC has authority over all interstate gas transportation, including transportation of bundled retail sales.

II. THE STATES' SECOND POINT RESTS UPON THE INVALID PREMISE THAT THE STATES CAN REGULATE WHOLESALE ELECTRIC POWER SALES

The States' argument that Order 888 improperly extends FERC jurisdiction to facilities used in local distribution of electric energy (Pet. 19-21) is equally misconceived. FPA section 201(b)(1) grants FERC jurisdiction over "all facilities" used by public utilities for the interstate transmission or wholesale sale of electric energy. The provision goes on to state that "except as specifically provided in this subchapter and subchapter III of this chapter," *i.e.*, Parts II and III of the FPA, FERC lacks jurisdiction "over facilities used in local distribution." As the D.C. Circuit correctly found, the FPA subordinates state jurisdiction over local distribution facilities to FERC jurisdiction over interstate transmission and sales at wholesale. Pet. App. C-37. Far from being an expansion of FERC jurisdiction, Order 888 confirms jurisdiction FERC and the FPC have for decades exercised over delivery over low-voltage power delivery facilities of wholesale sales of electric energy.

The necessary and faulty premise of States' position is that the states can regulate aspects of wholesale sales transported on low voltage distribution systems. States' position is irreconcilable with *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83, 89 (1927), finding the states powerless to regulate wholesale electric sales, and an "unbroken chain" of wholesale (gas) transport. This unbroken wholesale delivery chain exists under the FPA and bars states from regulating the low voltage delivery component of wholesale sales. *See United States v. Pub. Utils. Comm'n*, 345 U.S. 295, 310-11, 316 (1953) (neither FPA § 201(a) nor the use of local distribution facilities in effecting a sale preserve State commission jurisdiction over sales for resale in interstate commerce). "FERC's assertion of jurisdiction over all wholesale transmissions, regardless of

the nature of the facility, is clearly within the scope of its statutory authority." Pet. App. C-37.

The States' reliance on *Connecticut Light & Power Co. v. FPC,* 324 U.S. 515 (1945) is misplaced because the Court did not find that the states could regulate the low voltage distribution component of wholesale sales by public utilities. *See Arkansas Power & Light Co. v. FPC*, 368 F.2d 376, 383 & n.8 (8th Cir. 1966). Contrary to States' claim (Pet. 20), *Wisconsin-Michigan Power Co. v. FPC*, 197 F.2d 472, 477 (7th Cir. 1952), held that low-voltage delivery facilities used to deliver wholesale transactions were not "local distribution facilities" exempt from FPC jurisdiction because "at no point before the delivery to [the wholesale customer] has been completed, [is] interstate transmission terminated." Also, contrary to States' petition (Pet. 20), the reasoning of *Duke Power Co. v. FPC,* 401 F.2d 930, 942 (D.C. Cir. 1968), is that Duke's low voltage facilities would have been FPC "jurisdictional facilities ... [if they were] engaged in the ... sale at wholesale of electric energy in interstate commerce," but they were not. *Id.* at 950.

CONCLUSION

For these reasons, the petitions for writ of certiorari of the States and Dalton should be denied.

Respectfully submitted,

Robert C. McDiarmid
Counsel of Record
Cynthia S. Bogorad
Ben Finkelstein
Peter J. Hopkins

Supreme Court, U.S.
FILED
JAN 26 2001
OFFICE OF THE CLERK

Nos. 00-568, 00-800 and 00-809

In the Supreme Court of the United States

STATE OF NEW YORK, ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

BOARD OF WATER, LIGHT AND SINKING FUND COMMISSIONERS OF THE CITY OF DALTON, GEORGIA, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

ENRON POWER MARKETING, INC., PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

BARBARA D. UNDERWOOD
Acting Solicitor General
Counsel of Record
Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

DOUGLAS W. SMITH
General Counsel

CYNTHIA A. MARLETTE
Deputy General Counsel

SUSAN J. COURT
Associate Solicitor

TIMM L. ABENDROTH
Attorney
Federal Energy Regulatory Commission
Washington, D.C. 20426

29pp

QUESTIONS PRESENTED

In its Order No. 888 rulemaking, the Federal Energy Regulatory Commission found that public utilities subject to its jurisdiction under the Federal Power Act (FPA), 16 U.S.C. 792 *et seq.*, discriminated unlawfully in providing access to their electric transmission facilities. As a remedy, Order No. 888 requires them to unbundle their packaged wholesale electric energy service into separate energy sales and transmission services and to provide non-discriminatory access to their electric transmission systems in order to ensure "open access" to the interstate energy transmission grid and thereby facilitate competition in the national market for electric energy. The questions presented are:

1. Whether the Commission's open access regulations are permissible under Sections 205 and 206 of the FPA, 16 U.S.C. 824d and 824e.

2. Whether the Commission properly concluded that Section 201 of the FPA, 16 U.S.C. 824, authorizes the Commission to assert jurisdiction over interstate transmission service involved in a retail sale transaction where States have unbundled such transactions into separate transmission and sales services, but does not require the Commission to assert jurisdiction over transmission service that remains bundled with local retail sales and distribution service.

3. Whether Section 201 of the FPA authorizes the Commission to assert jurisdiction over facilities that may be used both for local distribution to retail customers and for transmission of electric energy to wholesale purchasers.

4. Whether Section 201 of the FPA bars the Commission from allowing utilities to recover certain stranded costs caused by the unbundling of retail electric service.

TABLE OF CONTENTS

	Page
Opinions below	2
Jurisdiction	2
Statement	2
Argument	10
Conclusion	23

TABLE OF AUTHORITIES

Cases:

American Trucking Ass'ns v. *Atchison, T. & S.F. Ry.*, 387 U.S. 397 (1967)	14
Arkansas Elec. Coop. Corp. v. *Arkansas Pub. Serv. Comm'n*, 461 U.S. 375 (1983)	16
Associated Gas Distribs. v. *FERC*, 824 F.2d 981 (D.C. Cir. 1987), cert. denied, 485 U.S. 1006 (1988)	8, 11, 12
CFTC v. *Schor*, 478 U.S. 833 (1986)	14
Connecticut Light & Power Co. v. *FPC*, 324 U.S. 515 (1945)	16, 17
EEOC v. *Commercial Office Prods. Co.*, 486 U.S. 107 (1988)	13
FDA v. *Brown & Williamson Tobacco Corp.*, 120 S. Ct. 1291 (2000)	14
FPC v. *Florida Power & Light Co.*, 404 U.S. 453 (1972)	8, 13
FPC v. *Louisiana Power & Light Co.*, 406 U.S. 621 (1972)	21
FPC v. *Southern Cal. Edison Co.*, 376 U.S. 205 (1964)	15, 16
Mississippi Power & Light Co. v. *Moore*, 487 U.S. 354 (1988)	14
Mississippi River Transmission Corp. v. *FERC*, 969 F.2d 1215 (D.C. Cir. 1992)	21

Cases—Continued: Page

Motor Vehicle Mfrs. Ass'n of United States v. *State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29 (1983) 14
NLRB v. *United Food & Commercial Workers Union*, 484 U.S. 112 (1987) 14
Northern States Power Co. v. *FERC*, 176 F.3d 1090 (8th Cir. 1999), cert. denied, 120 S. Ct. 1221 (2000) 15
Otter Tail Power Co. v. *United States*, 410 U.S. 366 (1973) 11
Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 10, 14
Reiter v. *Cooper*, 507 U.S. 258 (1993) 13

Statutes:

Federal Power Act, 16 U.S.C. 792 *et seq.*:
Pt. II, 16 U.S.C. 824-824m 2
§ 201, 16 U.S.C. 824 ..... 6, 13, 14, 15, 20
§ 201(a), 16 U.S.C. 824(a) 17
§ 201(b), 16 U.S.C. 824(b) 9, 12, 15, 17, 20, 21
§ 201(b)(1), 16 U.S.C. 824(b)(1) 2, 3, 17
§ 201(c), 16 U.S.C. 824(c) 3, 13
§ 201(e), 16 U.S.C. 824(e) 2
§ 201(f), 16 U.S.C. 824(f) 2
§ 205, 16 U.S.C. 824d 4, 8, 12
§ 205(b), 16 U.S.C. 824d(b) 3
§ 205(c), 16 U.S.C. 824d(c) 3
§ 206, 16 U.S.C. 824e 3, 4, 8, 12
§ 206(a), 16 U.S.C. 824e(a) 10
§ 211, 16 U.S.C. 824j 12, 15
§ 212(e)(1), 16 U.S.C. 824k(e)(1) 12
§ 212(h), 16 U.S.C. 824k(h) 14, 15, 18
Natural Gas Act, 15 U.S.C. 717 *et seq.*:
§ 1(b), 15 U.S.C. 717(b) 21
§ 5(a), 15 U.S.C. 717d(a) 11

Statutes—Continued: Page

§ 7(c), 15 U.S.C. 717f(c) 21
42 U.S.C. 7173(c) 11

In the Supreme Court of the United States

No. 00-568

STATE OF NEW YORK, ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

No. 00-800

BOARD OF WATER, LIGHT AND SINKING FUND COMMISSIONERS OF THE CITY OF DALTON, GEORGIA, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

No. 00-809

ENRON POWER MARKETING, INC., PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. C1-C121)[1] is reported at 225 F.3d 667. The relevant orders of the Federal Energy Regulatory Commission are reported as follows: Order No. 888, F.E.R.C. Stats. & Regs., Regulations Preambles January 1991-June 1996, ¶ 31,036; Order No. 888-A, 3 F.E.R.C. Stats. & Regs. ¶ 31,048; Order No. 888-B, 81 F.E.R.C. ¶ 61,248. Relevant portions of those orders are reprinted in Pet. App. D1-D125, E1-E120, and F1-F21; 00-809 Pet. App. 125a-369a, 371a-551a; 00-800 Pet. App. 1a-111a.

JURISDICTION

The judgment of the court of appeals (Pet. App. B1-B2) was entered on June 30, 2000. A petition for rehearing was denied on August 22, 2000 (Pet. App. A1-A2). The petition for a writ of certiorari in No. 00-568 was filed on October 12, 2000. The petitions in Nos. 00-800 and 00-809 were filed on November 20, 2000. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Part II of the Federal Power Act (FPA or the Act), 16 U.S.C. 824-824m, confers on the Federal Energy Regulatory Commission (FERC or the Commission) jurisdiction over rates, terms, and conditions of electric transmission service provided by public utilities in interstate commerce.[2] Section 201(b)(1) of the FPA

[1] Unless otherwise indicated, references to "Pet. App." are to the appendix to the certiorari petition in No. 00-568.

[2] Section 201(e), 16 U.S.C. 824(e), defines "public utility" as "any person who owns or operates facilities subject to the jurisdiction of the Commission." Section 201(f), 16 U.S.C. 824(f), excludes from FERC's jurisdiction companies owned by "the United States, a State or any political subdivision of a State," except as specifically provided.

authorizes the Commission to exercise jurisdiction over "the transmission of electric energy in interstate commerce," "the sale of electric energy at wholesale in interstate commerce," and "all facilities for such transmission or sale of electric energy." 16 U.S.C. 824(b)(1). Jurisdiction over "facilities used in local distribution or only for the transmission of electric energy in intrastate commerce" is left to the States. *Ibid.* Section 201(c) further provides that electric energy is transmitted in interstate commerce if it is "transmitted from a State and consumed at any point outside thereof." 16 U.S.C. 824(c).

Pursuant to Section 205(c) of the FPA, 16 U.S.C. 824d(c), public utilities subject to FERC's jurisdiction must file tariff schedules with FERC showing their rates and service terms, along with related contracts for jurisdictional service. Section 205(b) of the Act prohibits such utilities from "grant[ing] any undue preference or advantage to any person or subject[ing] any person to any undue prejudice or disadvantage." 16 U.S.C. 824d(b). Whenever the Commission finds that any rate charged by any such utility "for any transmission or sale," or that any utility's practice "affect[ing] such rate" is "unjust, unreasonable, unduly discriminatory or preferential," Section 206 of the Act directs FERC to prescribe a lawful rate or practice for the future. 16 U.S.C. 824e.

2. In recent years, the electric utility industry has evolved from a traditional, heavily regulated industry dominated by vertically integrated monopolies into a more competitive industry in which customers have choices as to their power suppliers. Pet. App. C8-C10.

A key impediment to developing a competitive wholesale market for electric power is the monopoly ownership of interstate transmission systems: a utility that controls access to transmission services can deny market access to competitors and favor its own generation in competing for buyers. *Id.* at C10. In Order No. 888, the Commission found, based on an extensive rulemaking record, that public utilities were denying or providing inferior access by others to their transmission service, in violation of the nondiscrimination provisions of Sections 205 and 206 of the Act. 00-809 Pet. App. 213a-218a.

As a remedy, Order No. 888 requires public utilities that own or control transmission facilities to offer transmission service to customers on terms comparable to the transmission service they use in serving their own power customers. Order No. 888 also prescribes certain minimum terms and conditions of service necessary to provide nondiscriminatory open-access service and requires utilities to file tariffs setting out those terms and conditions. Pet. App. C10-C11, D9. The Order further requires the unbundling of electric utilities' wholesale electricity product into separately priced sales and transmission services, and requires utilities to take transmission service for their own wholesale sales and purchases under the same open access tariff applicable to others. 00-809 Pet. App. 178a.

During the course of its rulemaking, the Commission addressed several issues concerning its jurisdiction over transmission of electric energy in light of the Act's provisions giving the States jurisdiction over local distribution and retail sales of electric energy. Among those issues was whether federal authority extended to the interstate transmission component of a public utility's sale of power to its retail customers. As the

Commission recognized, a growing number of States have permitted or required utilities that provide retail service to unbundle their services so that customers can purchase power from sources other than their historical suppliers. Pet. App. D7. Such unbundling, in turn, required the Commission to determine which transmission facilities and services would be subject to the nondiscriminatory tariffs of Order No. 888. The Commission resolved that jurisdictional question as follows:

> [W]e believe that when transmission is sold at retail as part and parcel of the delivered product called electric energy, the transaction is a sale of electric energy at retail. Under the FPA, the Commission's jurisdiction over sales of electric energy extends only to wholesale sales. However, when a retail transaction is broken into two products that are sold separately (perhaps by two different suppliers: an electric energy supplier and a transmission supplier), we believe the jurisdictional lines change. In this situation, the state clearly retains jurisdiction over the sale of the power. However, the unbundled transmission service involves *only* the provision of "transmission in interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission.

Id. at D44 (emphasis added). Given FERC's jurisdiction over unbundled transmission, the agency further distinguished between wholesale and retail transactions. In the wholesale situation, FERC asserted exclusive jurisdiction over the rates, terms, and conditions of all unbundled transmission service and the facilities used to provide the transmission, regardless of whether those facilities are labeled "transmission," "distribution" or "local distribution." *Id.* at D43-D44, D122, F8.

Order No. 888 thus requires public utilities offering such transmission to file transmission rate schedules with FERC that comply with its open-access rule, and provides that a share of the cost of transmission assets previously included in retail rate base will now be included in rate base subject to FERC's exclusive jurisdiction. *Id.* at D44-D53.

In the retail situation, however, FERC recognized both the States' continuing jurisdiction under Section 201 over "facilities used in local distribution," and the absence of any bright line to distinguish those facilities from interstate transmission facilities. The Commission therefore adopted a test to distinguish between transmission facilities and local distribution facilities, based on the function and technical characteristics of the facilities. Pet. App. D19-D20.[3] FERC also stated that it would defer to state recommendations in such matters, including where to draw the jurisdictional line between transmission and local distribution under FERC's test. *Id.* at D41-D52.

FERC further clarified several other aspects of its exercise of jurisdiction over unbundled transmission for

---

[3] The test takes into account the following factors:

(1) Local distribution facilities are normally in close proximity to retail customers; (2) Local distribution facilities are primarily radial in character; (3) Power flows into local distribution systems; it rarely, if ever, flows out; (4) When power enters a local distribution system, it is not reconsigned or transported on to some other market; (5) Power entering a local distribution system is consumed in a comparatively restricted geographical area; (6) Meters are based at the transmission/local distribution interface to measure flows into the local distribution system; (7) Local distribution systems will be of reduced voltage.

Pet. App. D19-D20.

retail sale. First, FERC emphasized that in exercising jurisdiction over the rates, terms, and conditions of the transmission component of unbundled retail transactions, it was not asserting authority either to order the unbundling of retail transactions or to order retail transmission to an ultimate consumer. Rather, its jurisdiction attaches only *if* retail transmission has been unbundled from the retail sale, either voluntarily by the utility or as a result of a state-ordered retail program. Pet. App. D44. Second, FERC clarified that its jurisdiction over the rates, terms, and conditions of unbundled retail transmission would not affect matters traditionally left to the States, "including authority to regulate the vast majority of generation asset costs, the siting of generation and transmission facilities, and decisions regarding retail service territories." *Id.* at D12; see also *id.* at D46 & n.544.

Order No. 888 also addresses problems created by "stranded costs," *i.e.*, a utility's sunk plant and other costs that it cannot recoup when customers, who previously took bundled service from the utility, take advantage of open-access transmission to purchase cheaper power from other suppliers. Pet. App. C11. Order No. 888 affords utilities an opportunity to recover such costs from a former customer that purchased its power requirements from the utility, but only if (a) the customer uses the former utility's transmission system to reach the new supplier, and (b) the utility shows a "reasonable expectation" that it would have continued to serve that customer beyond the end of its contract term. *Id.* at C11, C42-C48, D53-D54. With respect to costs stranded where retail customers are able to find new suppliers as a result of state retail unbundling, FERC recognized the primacy of state jurisdiction, and therefore took the position

that it would serve as a forum for cost recovery only if a state regulator lacked authority to do so and the departing customer uses a FERC transmission tariff to reach its new supplier. *Id.* at D80-D84, E91-E96.[4]

3. In a unanimous per curiam decision, the court of appeals upheld FERC's rules "in nearly all respects." Pet. App. C8.[5] The court first held that FERC had authority to require open access by virtue of its authority under Sections 205 and 206 to remedy undue discrimination by public utilities. *Id.* at C16-C19. The court of appeals relied in part on its decision in *Associated Gas Distributors* v. *FERC*, 824 F.2d 981 (D.C. Cir. 1987), cert. denied, 485 U.S. 1006 (1988), in which it upheld a similar open-access requirement imposed by FERC on natural gas transportation under parallel provisions of the Natural Gas Act (NGA). See Pet. App. C17-C19, C21-C22. The court further held that FERC permissibly relied on generic findings of undue discrimination by utilities, and that FERC therefore was not required to find each individual utility's rates or practices unlawful. *Id.* at C19-C22.

The court also affirmed the jurisdictional basis for Order No. 888. Pet. App. C26-C38. The court explained that "[b]oth FPA [Sections] 201(a) and (b) clearly and unambiguously confer upon FERC jurisdiction over the 'transmission of electric energy in interstate commerce.'" *Id.* at C30-C31. The court

[4] FERC also stated that it would serve as the primary forum for recovery of stranded costs where former retail customers become wholesale customers through what is known as municipalization or municipal annexation. Pet. App. C79.

[5] The court remanded to the agency to explain its treatment of certain stranded energy costs and to provide a reasonable cap on certain contract extensions. Pet. App. C12.

observed (*id.* at C31-C32) that this Court held in *FPC* v. *Florida Power & Light Co.*, 404 U.S. 453 (1972), that the very interconnection of utilities to the interstate grid results in a commingling of electricity and energy flows across state lines in interstate commerce, and under that precedent, "the FPA gives FERC the authority to regulate the transmissions at issue here, whether retail or wholesale." Pet. App. C33. The court also sustained FERC's decision not to assert jurisdiction over retail transmission that remains bundled with retail sales, reasoning that the Act is ambiguous with respect to the issue and that FERC's decision "represents a statutorily permissible policy choice to which [the court] must * * * defer under *Chevron*." *Id.* at C34. At the same time, the court rejected the challenge by certain States to FERC's exercise of jurisdiction over local distribution facilities that are used in wholesale transactions. The court concluded that since "FPA [Section] 201(a) makes clear that all aspects of wholesale sales are subject to federal regulation, regardless of the facilities used[,] FERC's assertion of jurisdiction over all wholesale transmissions, regardless of the nature of the facility, is clearly within the scope of its statutory authority." *Id.* at C37.

The court further held that FERC could permit recovery of retail stranded costs, in situations in which customers take advantage of state-ordered wheeling and state commissions lack the authority to award recovery of such costs. The court reasoned that "costs" are not jurisdictional and, thus, while Section 201(b) of the Act denies FERC jurisdiction over "facilities used for the generation of electric energy," 16 U.S.C. 824(b), "that provision does not necessarily prevent FERC from including *costs* relating to generating facilities in

transmission *rates*, over which FERC indisputably has jurisdiction." Pet. App. C81.

ARGUMENT

1. a. Petitioner Board of Water, Light and Sinking Fund Commissioners of the City of Dalton, Georgia (Dalton) argues (00-800 Pet. 7-10, 14-22) that FERC's reliance on generic findings of undue discrimination and its open-access remedy conflict with Section 206(a)'s requirement that FERC must premise a remedy on a finding that each individual utility's practice "affecting" a rate "is" unduly discriminatory.[6] That contention lacks merit.

FERC specifically concluded that "there is more than sufficient reason to believe that transmission monopolists *currently* engage in unduly discriminatory practices, and that they will continue to engage in unduly discriminatory practices, unless [FERC] fashion[s] a remedy to eliminate their ability and incentive to do so." 00-809 Pet. App. 216a (emphasis added). FERC based that finding on its own experience in reviewing applications and complaints, public comments presenting examples and allegations of widespread discrimination, and its determinations concerning the existence of systemic monopoly conditions and the economic self-interest of transmission monopolists–as well as FERC's expert prediction that such discrimination would likely

[6] Dalton also suggests (00-800 Pet. 16-18) that its own circumstances justify the conclusion that FERC erred in making generic findings of discrimination and imposing a generic remedy. The court of appeals, however, found that contention not ripe for review, Pet. App. C24, and Dalton does not challenge that ruling in this Court.

increase in the future. Pet. App. C20-C21; 00-809 Pet. App. 209a-218a, 213a-214a, 315a-331a.[7]

The court of appeals therefore properly held that the agency's rules need not be premised on "specific findings" for each individual company where, as here, the agency's factual determinations are reasonable. Pet. App. C21. The court of appeals noted that it had previously upheld FERC's authority to proceed by rulemaking in exercising its parallel authority to address discriminatory practices under Section 5(a) of the NGA, 15 U.S.C. 717d(a), that Congress had ratified that approach in 42 U.S.C. 7173(c), and that the court had rejected similar challenges to FERC's ordering of open-access in the natural gas industry in *Associated Gas Distributors*, 824 F.2d at 1008. The court of appeals' decision upholding FERC's exercise of that settled authority in Order No. 888 presents no issue warranting this Court's review.

b. Dalton also contends (00-800 Pet. 22-27) that Order No. 888 conflicts with *Otter Tail Power Co.* v. *United States*, 410 U.S. 366 (1973). In that case, this Court held that the FPA did not preempt an antitrust remedy that ordered involuntary wheeling (*i.e.*, mandatory transmission for a third party), reasoning that "[s]o far as wheeling is concerned, there is no authority

[7] It is well-settled that an agency may rely on established economic principles in promulgating rules. See, *e.g.*, *Permian Basin Area Rate Cases*, 390 U.S. 747, 792-795 (1968) (upholding Commission's rejection of contract pricing based on considerations of, inter alia, "market imperfections" and a "monopsonistic environment"); see also Pet. App. C22. Dalton does not challenge either that proposition or the Commission's authority to proceed by rulemaking rather than case-by-case adjudication. See 42 U.S.C. 7173(c) ("[T]he establishment of rates and charges under [the FPA] * * * may be conducted by rulemaking procedures.").

granted the Commission under Part II of the Federal Power Act to order it, for the bills originally introduced contained common carrier provisions which were deleted." *Id.* at 375. As the court of appeals explained, however, *Otter Tail* does not address whether the Commission may order wheeling in the exercise of its authority under Sections 205 and 206 to remedy undue discrimination. Pet. App. C18-C19. Those provisions specifically confer on FERC the authority to prescribe rates and practices upon a finding of undue discrimination, and the court of appeals correctly held that FERC has reasonably construed those provisions as conferring broad authority to remedy unduly discriminatory behavior by an open-access requirement. *Id.* at C19. As the court of appeals also pointed out (C18-C19), that court rejected similar arguments based on *Otter Tail* in *Associated Gas Distributors* some 13 years ago. See 824 F.2d at 998-999. In this respect as well, then, the court of appeals' decision breaks no new ground and presents no issue warranting review by this Court.[8]

2. The petitioners in No. 00-568 are nine state regulatory commissions (the States) that challenge (Pet. 12-19) FERC's jurisdiction over the transmission service

[8] There similarly is no merit to Dalton's claim (00-800 Pet. 26-27) that the Commission's open-access rule is inconsistent with the authority to order wheeling on a case-by-case basis under Section 211 of the FPA, 16 U.S.C. 824j. Nothing in Section 211 undermines the Commission's remedial authority under Section 206. See 16 U.S.C. 824k(e)(1) (Section 211 "shall not be construed as limiting or impairing any authority of the Commission under any other provision of law."); see also 00-800 Pet. App. 69a-70a. As the Commission explained, the authority conferred by Section 211 was simply inadequate to meet the industry-wide conditions it sought to address in Order No. 888. *Id.* at 45a-46a.

involved in unbundled retail transactions. The court of appeals properly rejected their contentions.

a. Section 201(b) explicitly gives FERC jurisdiction over all "transmission of electric energy in interstate commerce" and "all facilities for such transmission," regardless of whether the transmission is part of a wholesale or retail transaction. In *FPC* v. *Florida Power & Light Co.*, 404 U.S. 453, 462-463 (1972), this Court recognized that when a utility's transmission lines connect to an interstate grid, the utility's energy commingles with that of other utilities so that inevitably some energy is transmitted across state lines and becomes interstate in nature.[9] The court of appeals therefore correctly concluded that "the FPA gives FERC the authority to regulate the transmissions at issue here, whether retail or wholesale." Pet. App. C33. The States' arguments to the contrary lack merit.

i. The States argue (00-568 Pet. 12) that the court of appeals improperly deferred to the Commission's view of its jurisdiction. The court held, however, that it was bound by this Court's interpretation in *Florida Power & Light* of "interstate transmission" under Section 201, and held only alternatively that it would defer to

[9] For that reason, the States' reliance (00-568 Pet. 15-16) on Section 201(c), 16 U.S.C. 824(c), which states that energy is transmitted in interstate commerce if "transmitted from a State and consumed at any point outside thereof," is misplaced. With transmission interconnection, some of the electricity generated and transmitted in one State is almost inevitably consumed "outside thereof." That conclusion, however, does not create a null set of "intrastate transmission" under the FPA, because utilities may have no interconnection that would permit the physical transmission of power outside of a State, such as in Alaska, Hawaii, and most areas of Texas. See Pet. App. D43 n.541.

FERC's interpretation of its jurisdictional authority. See Pet. App. C33. In any event, this Court repeatedly has deferred to an agency's reasonable interpretation of a statute affecting the scope of its jurisdiction. See, *e.g.*, *Reiter* v. *Cooper*, 507 U.S. 258, 269 (1993); *EEOC* v. *Commercial Office Prods. Co.*, 486 U.S. 107, 115 (1988); *NLRB* v. *United Food & Commercial Workers Union*, 484 U.S. 112, 123 (1987); *CFTC* v. *Schor*, 478 U.S. 833, 845 (1986); see also *Mississippi Power & Light Co.* v. *Moore*, 487 U.S. 354, 380-382 (1988) (Scalia, J., concurring in the judgment) (collecting cases on question of deference to agency's interpretation of statute concerning its jurisdiction).

ii. The States argue (00-568 Pet. 14-15) that Order No. 888 conflicts with the statements by FERC and the Federal Power Commission (FPC) in congressional hearings and briefs to this Court that Section 201 does not extend the Commission's jurisdiction to retail sales. Neither FERC nor the FPC, however, has ever taken a position on the jurisdictional issues presented in this case. In Order No. 888, FERC addressed for the first time its view of the jurisdictional consequences of dramatic changes since enactment of the FPA, *i.e.*, the increase in competition in the electric utility industry and the advent of unbundled services. In light of those economic realities, FERC was well within its broad authority "to 'adapt [its] rules and policies to the demands of changing circumstances.'" *FDA* v. *Brown & Williamson Tobacco Corp.*, 120 S. Ct. 1291, 1313 (2000) (quoting *Motor Vehicle Mfrs. Ass'n of United States* v. *State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 42, 103 (1983) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 784 (1968))); see also *American Trucking Ass'ns* v. *Atchison, T.& S.F. Ry.*, 387 U.S. 397, 415 (1967) ("[T]he Commission, faced with new

developments, or in light of reconsideration of the relevant facts and its mandate, may alter its past interpretation.").

iii. The States further argue (00-568 Pet. 16) that Order No. 888 conflicts with Section 212(h) of the Act, 16 U.S.C. 824k(h), which sets forth the terms, conditions, and limitations on FERC's authority under Section 211, 16 U.S.C. 824j, to require transmission wheeling on a case-by-case basis, and provides that nothing in Section 212(h) "shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an ultimate consumer." That provision has no application here, and in no way purports to limit FERC's jurisdiction under Section 201(b) over the rates, terms, and conditions of the transmission of electric energy in interstate commerce. Section 212(h) simply prohibits FERC from ordering transmission directly to an ultimate consumer, and in the challenged orders FERC disavowed any power to do so. Pet. App. D44. Moreover, when a utility engages in retail unbundling, either voluntarily or as required by state law, the States retain authority under Order No. 888 over local matters such as power production, customer service, and local reliability. *Id.* at D44-D46.

iv. The States assert (00-568 Pet. 17) that the Commission's exercise of jurisdiction over the transmission component on an unbundled retail transaction conflicts with this Court's observation in *FPC* v. *Southern California Edison Co.*, 376 U.S. 205, 215 (1964), that Section 201 creates a "bright-line" jurisdictional test between wholesale (*i.e.*, sales for resale) and retail (*i.e.*, direct) sales of energy. Order No. 888, however, does not depart from that test, but rather requires FERC to distinguish between facilities used for *transmission* and

facilities used for *local distribution*.[10] Indeed, the Court in *Southern California Edison*, 376 U.S. at 210 n.6, acknowledged the absence of such a bright-line distinction in that respect, concluding that the issue "involves a question of fact to be decided by [the agency] as an original matter." See also *Connecticut Light & Power Co.* v. *FPC*, 324 U.S. 515, 531-536 (1945).[11]

v. The States argue (00-568 Pet. 18) that, as a policy matter, Order No. 888 undermines competition because it will encourage States not to order retail unbundling for fear of losing jurisdiction over transmissions associated with retail transactions. That contention erroneously assumes that States will not weigh their consumers' best interests in deciding for, or against, retail wheeling, but will be concerned only with protecting their own jurisdiction. In any event, the States have made no showing that Order No. 888 actually has deterred any State from ordering retail

[10] Contrary to the States' suggestion (00-568 Pet. 17), the decision below does not conflict with *Northern States Power Co.* v. *FERC*, 176 F.3d 1090, 1096 (8th Cir. 1999), cert. denied, 120 S. Ct. 1221 (2000), which addressed aspects of Order No. 888's curtailment provisions. The decision in that case did not address FERC's jurisdiction over unbundled retail transmissions, facilities used in wholesale transactions, or stranded costs caused by FERC's open-access requirement.

[11] The States' reliance (00-568 Pet. 18) on *Arkansas Electric Cooperative Corp.* v. *Arkansas Public Service Comm'n*, 461 U.S. 375, 394 (1983), for the proposition that "mere interconnection of electric utilities is not enough to defeat state jurisdiction" is likewise misplaced. In that case, the Court had already determined that the FPA did not cover the transactions by rural power cooperatives that were at issue, before finding that regulation of wholesale rates was within the legitimate scope of local interests, notwithstanding a connection to the interstate grid. *Id.* at 384-385.

unbundling, and we have been advised by FERC that many States have ordered retail unbundling even after Order No. 888 became effective.

b. The States also challenge (00-568 Pet. 19-21) FERC's exercise of jurisdiction over local distribution facilities used in wholesale transmission transactions. The court of appeals properly rejected that argument, reasoning that Section 201(b) limits FERC jurisdiction over local distribution facilities "*except* as specifically provided in this subchapter and subchapter III," 16 U.S.C. 824(b)(1) (emphasis added), and Section 201(a) "makes clear that all aspects of wholesale sales are subject to federal regulation, regardless of the facilities used." Pet. App. C37. Consistent with Section 201(b)'s reservation of state jurisdiction over "facilities used in local distribution," Order No. 888 preserves the traditional areas of state regulation. Thus, where a public utility is transmitting unbundled energy to an end user —*i.e.*, where the transmission is connected to a retail rather than a wholesale transaction—Order No. 888 acknowledges that some of the facilities involved are local distribution facilities subject to state jurisdiction, and Order No. 888 establishes a test for defining the jurisdictional line on a case-by-case basis. *Id.* at D19-D20.

For similar reasons, the States err in arguing (00-568 Pet. 20) that Order No. 888 conflicts with this Court's observation in *Connecticut Light & Power Co.*, 324 U.S. at 531, that Congress's preservation of state jurisdiction in Section 201(b) over "facilities used in local distribution" is "a limitation on jurisdiction and a legal standard that must be given effect," regardless of whether the facility carries out-of-state energy. In Order No. 888, FERC has exercised jurisdiction over those facilities used in wholesale transactions, and it

has established a test to distinguish those facilities used for local distribution from those used for unbundled retail transmission. As the court of appeals concluded, Order No. 888 reasonably "recognizes the current reality that many primarily retail utilities engage in both local distribution and interstate transmissions, and seeks through the seven factors to discern each facility's primary function." Pet. App. C38.

There is likewise no merit to the States' contention (00-568 Pet. 19, 21) that the court of appeals' ruling upholding FERC's authority over all facilities used in wholesale transactions allows "FERC to usurp state power to ensure reliable local distribution," permits utilities to evade state regulation, and violates Congress's ban in Section 212(h), 16 U.S.C. 824k(h), on sham wholesale transactions. FERC stressed in its rulemaking that Order No. 888 would not affect traditional state jurisdiction over local service concerns, including reliability. Pet. App. D44-D53. Order No. 888 also does not affect the States' ability to set bundled retail rates, including a cost component reflecting use of facilities to deliver power to the ultimate consumer. FERC further stated that it would address on a case-by-case basis the possibility that transactions may be structured to avoid federal regulation, see, *e.g.*, *id.* at D52, and the States offer no reason to believe that FERC would approve a sham transaction barred by Section 212(h).

c. The States finally argue (00-568 Pet. 22-24) that FERC lacks the "backstop" authority to address requests for recovery of stranded costs arising out of state-ordered retail unbundling in the event that a state regulator lacks authority to provide for such recovery. The court of appeals correctly held, however, that the inclusion of stranded costs relating to generation facilities in transmission rates is a legitimate exercise of FERC's authority over transmission rates, because "[r]ates are jurisdictional; costs are not." Pet. App. C80-C81. For example, both FERC and a state commission may legitimately take the exact same plant costs into consideration in setting rates within their respective bailiwicks for setting wholesale and retail rates. *Id.* at C81. As the court explained, if a utility seeks to recover retail stranded costs in its FERC-jurisdictional transmission rates, FERC will exercise its traditional cost-of-service ratemaking jurisdiction to review those costs. *Ibid.* As the court further explained, both retail and wholesale stranded costs can be viewed as "costs" of providing transmission services because, while "such costs are not a cost of operating the physical transmission system, nevertheless, they are an economic cost incurred as a result of being required to provide retail transmission." *Id.* at C83 (quoting *id.* at E94 n.708). While agreeing that generation-related retail costs are not typically costs relating to transmission services, the court correctly held that "the fundamental changes wrought by state-ordered retail wheeling, as well as the narrow circumstances in which FERC will consider stranded-cost recovery claims, justify the conclusion that these costs are costs of providing transmission service." *Ibid.*[12]

[12] The States similarly err in challenging (00-809 Pet. 24) FERC's exercise of jurisdiction over stranded costs in certain so-called "retail-turned-wholesale" situations where, for example, a municipal utility becomes the conduit by which a retail customer can switch from its historical local utility power supplier, using the local utility's FERC open access transmission tariff to reach a new supplier. Pet. App. D64-D65, E71-E78, F16-F19; 00-809 Pet. App. 499a n.479. In those situations, assuming the utility carries its burden of proof, FERC will provide for recovery through a customer-

FERC, moreover, has stated that "[t]he only circumstance" in which it would "entertain requests" to recover stranded costs relating to retail wheeling "is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required." Pet. App. C79. No such claim for recovery has been presented to the Commission in the almost five years since it issued Order No. 888, and the hypothetical circumstance of a state regulator not having authority to address the problem may never arise.

3. Petitioner Enron Power Marketing, Inc. argues (00-809 Pet. 11-16) that Section 201(b) requires the Commission to assert jurisdiction over transmission of electric energy that remains part of a bundled retail sale. The court of appeals, however, correctly declined to hold that the Commission must treat all bundled retail sales as separate sales and transmission services and assert jurisdiction over the transmission component of the transactions.

Although Section 201 clearly gives FERC jurisdiction over transmission in interstate commerce and wholesale sales, and the Act gives States jurisdiction over local distribution facilities and retail sales, the "statute is much less clear about exactly where the lines between those activities are to be drawn." Pet.

---

specific surcharge to be added to the transmission rate. Pet. App. E85. The court of appeals correctly upheld FERC's authority in that respect, reasoning that "FERC's exclusive jurisdiction over all aspects of wholesale sales gives FERC all the authority it needs to include generation-related costs in rates, including even costs originally incurred to provide retail service." *Id.* at C91. Moreover, "[a]s in the retail wheeling context, these stranded costs are properly viewed as 'costs' of the former supplying utility's provision of open access transmission service." *Ibid.*

App. C34. The court of appeals therefore correctly held that "[a] regulator could reasonably construe transmissions bundled with generation and delivery services and sold to a consumer for a single charge as either transmission services in interstate commerce," over which FERC has jurisdiction, "or as an integral component of a retail sale," over which the States have jurisdiction. In those circumstances, the court properly deferred to FERC's decision to treat bundled transmission as part of retail sales as "a statutorily permissible policy choice." *Ibid.*[13]

Enron also contends (00-809 Pet. 17-22) that FERC's decision not to assert jurisdiction over bundled retail transmissions will have a detrimental impact on nondiscriminatory access to transmission services. FERC specifically considered the competing policy issues at stake, and permissibly determined that an exercise of its jurisdiction was not necessary to achieve nondiscriminatory open access to transmission services. In its

---

[13] Enron argues (00-809 Pet. 14-15) that FERC's interpretation conflicts with this Court's interpretation in *FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972), of Section 1(b) of the NGA, 15 U.S.C. 717(b), a provision parallel to Section 201(b) of FPA. That case did not address, however, the Commission's authority to regulate transmission bundled with retail sales, but simply held that the reservation to the States of jurisdiction over retail natural gas sales did not preclude the Commission from exercising jurisdiction over the curtailment of natural gas deliveries in times of shortage. 406 U.S. at 623. Enron similarly errs in relying (00-809 Pet. 15-16.) on the D.C. Circuit's decision in *Mississippi River Transmission Corp.* v. *FERC*, 969 F.2d 1215 (1992), which held that FERC may regulate the transportation embedded in a retail natural gas sale. That decision construed FERC's authority to issue a certificate for pipeline service under Section 7(c) of the NGA, 15 U.S.C. 717f(c), a provision with no parallel in the FPA.

Notice of Proposed Rulemaking, the Commission explained that its approach "raises the possibility that the quality of transmission service for retail purposes will be superior to the quality of transmission service offered for wholesale purposes," 00-809 Pet. App. 634a, and therefore sought public comment on how its "bifurcated approach would affect the public utility's incentives to provide nondiscriminatory open access wholesale transmission service," *id.* at 635a.

In its Final Rule, the Commission explained that "[t]he majority of commenters addressing this issue believe that unbundling retail services is unnecessary to establish a competitive market and to achieve nondiscriminatory open access transmission." 00-809 Pet. App. 234a. After reviewing those comments, as well as views of commenters opposing the Commission's approach, the Commission concluded that "[a]lthough the unbundling of retail transmission and generation, as well as wholesale transmission and generation, would be helpful in achieving comparability," the Commission did "not believe it is necessary." *Id.* at 235a. That policy judgment is reasonable, and does not warrant this Court's review.[14]

[14] In the event that the Court were to grant the States' petition challenging Order No. 888's exercise of jurisdiction, the Commission would not oppose the Court's granting of Enron's petition as well.

CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted.

BARBARA D. UNDERWOOD
Acting Solicitor General

DOUGLAS W. SMITH
General Counsel

CYNTHIA A. MARLETTE
Deputy General Counsel

SUSAN J. COURT
Associate Solicitor

TIMM L. ABENDROTH
Attorney
Federal Energy Regulatory Commission

JANUARY 2001

Supreme Court, U.S.
FILED

FEB 2 2001

OFFICE OF THE CLERK

(S)

No. 00-568

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK and THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioners,

-v-

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

REPLY BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

LAWRENCE G. MALONE*
General Counsel
JONATHAN D. FEINBERG
DIANE T. DEAN
Assistant Counsel
NYS-Dept. of Public Service
Public Service Commission
3 Empire State Plaza
Albany, NY 12223-1350
(518) 474-2510

**Counsel of Record*

February 2, 2001

THE REPORTER COMPANY, *Printers and Publishers, Inc.*
181 Delaware Street, Walton, NY 13856—800-252-7181
(3112 – 2001)

Printed on Recycled Paper

800

TABLE OF CONTENTS

Page

POINT I 1

FERC AND ITS SUPPORTERS HAVE FAILED TO ANSWER THE STATES' SHOWING THAT THE D.C. CIRCUIT APPLIED THE WRONG STANDARD OF REVIEW, MISREAD FLORIDA POWER & LIGHT, RAN AFOUL OF TEACHINGS OF THIS COURT, AND IGNORED THE WILL OF CONGRESS IN AFFIRMING FERC'S PREEMPTION OF STATE REGULATION OF THE TRANSMISSION OF ELECTRICITY FROM SELLERS TO RETAIL CUSTOMERS IN THE SAME STATE 1

A. Florida Power & Light/Deference 2

B. FERC's Reversal of Position 5

C. Section 212(h) 6

D. The Retail/Wholesale "Bright Line" 6

E. Order 888's Impracticality 7

POINT II 7

FERC HAS FAILED TO JUSTIFY THE D.C. CIRCUIT'S AFFIRMANCE OF ITS PRE-EMPTION OF STATE REGULATION OF LOCAL DISTRIBUTION FACILITIES USED FOR WHOLESALE SALES 7

Page

POINT III 9

FERC AND ITS SUPPORTERS HAVE FAILED TO ANSWER THE STATES' DEMONSTRATION THAT THE D.C. CIRCUIT'S TREATMENT OF STRANDED COSTS WAS ERRONEOUS 9

CONCLUSION 10

TABLE OF AUTHORITIES

Cases **Page**

Chemehuevi Tribe of Indians v. Federal Power Commission, 420 U.S. 395 (1975) 1

Connecticut Light & Power v. Federal Power Commission, 324 U.S. 515 (1944) 3, 7, 8

Duke Power Company v. Federal Power Commission, 401 F.2d 930 (D.C. Cir. 1968) 9

Federal Power Comm'n v. Conway Corp., 426 U.S. 271 (1976) 9

Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205 (1964) 6, 8

Federal Power Commission v. Florida Power & Light Co., 404 U.S. 453 (1972) ..... *passim*

Food and Drug Administration v. Brown & Williamson Tobacco Corp., __U.S.__, 120 S. Ct. 1291 (2000) 5

Hillsborough County, Florida v. Automated Medical Laboratories, 471 U.S. 715 (1985) 3, 4

Jersey Central Power & Light Co. v. Federal Power Commission, 319 U.S. 61 (1943) 3

Louisiana Public Service Commission v. Federal Communications Commission,, 476 U.S. 355 (1986) 10

Page

Mississippi Power & Light Co. v. Mississippi ex rel Moore, 487 U.S. 354 (1988) 4

Watt, Secretary Of The Interior v. Alaska, 451 U.S. 259 (1981) 5

Statutes:

FPA § 201 [16 U.S.C. § 824] 4,5

FPA § 201(a) [16 U.S.C. § 824(a)] 3, 7, 8

FPA § 201(b) [16 U.S.C. § 824(b)] 1, 6, 7, 8

FPA § 201(c) [16 U.S.C. § 824(c)] 2, 3, 7

FPA § 212(h) [16 U.S.C. § 824(h)] 6, 7

FPA § 301 [16 U.S.C. § 825] 2

The States' October 11, 2000 petition for a writ of certiorari offers numerous reasons why the D.C. Circuit's decision affirming Federal Energy Regulatory Commission (FERC) Order 888 warrants review. Because FERC and its supporters utterly fail to refute the States' arguments – and, in some instances, do not even address them – their briefs inadvertently provide additional support for the States' petition.

POINT I

FERC AND ITS SUPPORTERS HAVE FAILED TO ANSWER THE STATES' SHOWING THAT THE D.C. CIRCUIT APPLIED THE WRONG STANDARD OF REVIEW, MISREAD FLORIDA POWER & LIGHT, RAN AFOUL OF TEACHINGS OF THIS COURT, AND IGNORED THE WILL OF CONGRESS IN AFFIRMING FERC'S PREEMPTION OF STATE REGULATION OF THE TRANSMISSION OF ELECTRICITY FROM SELLERS TO RETAIL CUSTOMERS IN THE SAME STATE.

The D.C. Circuit affirmed FERC's preemption of "retail transmission" (Q3)[1] by reading this Court's decision in Federal Power Comm'n v. Florida Power & Light Co. (FP&L), 404 U.S. 453 (1972), as declaring all transmissions of electricity to be interstate (C32-C33). In the alternative, the Court held that FERC's conclusion that § 201(b) of the Federal Power Act (FPA) granted FERC jurisdiction over all transmissions of electric energy outside of Alaska, Hawaii and Texas warranted deference (C33-C34).

The States' petition describes numerous errors in the D.C. Circuit's decision (Pet. 10-19). FERC does not even attempt to answer several of the States' points, including the D.C. Circuit's erroneous standard of review, the Court's failure to adhere to Chemehuevi Tribe of Indians v. Federal Power Comm'n, 420

---

[1] (Letter-number) refers to relevant pages of Petitioners' Appendix.

U.S. 395, 422-424 (1975), or Order 888's inconsistency with state/federal antitrust jurisprudence. The issues that FERC does address are examined below.

A. Florida Power & Light/Deference

FERC, and the D.C. Circuit, read this Court's decision in FP&L as holding that because electrons move elusively throughout the transmission system, all energy should be assumed to be in interstate commerce – even transmission from a generator in the middle of Nebraska to a retail customer 50 feet away. The issue in FP&L was whether the ninth largest electric utility in the United States was a "public utility" under § 301 of the FPA and, therefore, was subject to FERC's accounting jurisdiction. Did its facilities transmit a single electron that was consumed in a state other than in which it was generated (404 U.S. at 461 n.10)? If so, FP&L was a "public utility" and FERC could look at its books. In holding for FERC, the Court found that due to the elusive character of electricity, one or more of the electrons carried by FP&L near the Georgia/Florida border had to oscillate across state lines. The case has no application to FERC's authority to regulate retail transmission because, as FERC emphasized in its briefs to the Court, FERC was not trying to regulate any FP&L service (404 U.S. at 461).

Thus, FP&L does not stand for the proposition that all electrons transmitted to FP&L's retail customers were in interstate commerce. Nor does it suggest they were produced in a different state – the appropriate test under FPA § 201(c) for whether FERC would be able to regulate FP&L's retail transmissions.[2]

---

[2] Arguing that FP&L holds that all energy on an integrated grid is a commingled stream of electrons from multiple sources, the Transmission Access Policy Study (TAPS) group claims it is impossible to have direct intrastate transmission from a generator to a customer (TAPS 2-3). While the Court's opinion in FP&L recognized it was, indeed, possible to identify which utilities were generating which loads (404 U.S. at 461-462), TAPS'

The D.C. Circuit's error becomes even more apparent when FP&L is read in concert with Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61 (1943). In Jersey Central, this Court held that: "although a company may be a public utility under subsection (e), all of its transactions do not thereby fall under the regulatory power of the Commission." 319 U.S. at 73. Section 201(a)'s "limitation is directed at generation, transmission and sale" (emphasis added) (319 U.S. at 74). Because § 201(a) prohibits FERC from regulating any activity previously regulated by the states and the states were regulating retail transmission when the FPA was enacted (I4, P3), § 201(a) prohibits FERC from regulating retail transmission. The D.C. Circuit has misread FP&L.

FERC cites this Court's deference to agency interpretations of enabling legislation as support for the D.C. Circuit's deference to FERC's rejection of § 201(a)'s limiting language (FERC 14). Its argument is particularly baseless in light of FERC's failure even to take issue with the following: (1) in Hillsborough County Florida v. Automated Medical Laboratories, 471 U.S. 715 (1985), this Court held that an agency cannot preempt pre-existing state regulation unless preemption is shown to be "the clear and manifest purpose of Congress" (Pet. 10); (2) the States were, in fact, regulating retail transmission when the 1934 Act was passed (I4, H14) and Congress had no intention of disturbing this state regulation (Connecticut Light & Power Co. v. Federal Power Comm'n (CL&P), 324 U.S. 515, 526 (1944); (L10, L12, P4, P23) (Pet. 11); and (3) by FERC's own admission, the FPA does not evidence a clear and manifest purpose of Congress to allow preemption of retail transmission (D100)

---

contention is, nonetheless, a red herring. Inasmuch as Congress has defined intrastate transmissions as those between buyers and sellers in the same state (§ 201[c]) and neither bilateral contracts nor intrastate retail tariffs have ever relied on a "tracing" of electrons for their legal efficacy, the elusive nature of electrons is not relevant to FERC's power to preempt state regulation of retail transmission.

["The above legislative history on section 201 . . . does not provide any definitive answers to the questions raised."]. Inasmuch as the D.C. Circuit decision is inconsistent with Hillsborough and FERC has not even attempted to defend the Court's inconsistency, its call for deference rings hollow (see Pet. 8, 9, 11).

TAPS describes the States as contending that Hillsborough raises the preemption bar whenever a federal statute "reserves certain powers to the states" (TAPS 4). Building on its erroneous description of the States' petition, TAPS then reasons that because Justice Scalia's concurring opinion in Mississippi Power & Light Co. v. Mississippi ex rel. Moore (MP&L), 487 U.S. 354, 380-381 (1988), endorsed deference to FERC's reading of the FPA, which reserves certain power to the states, Hillsborough has been undermined (TAPS 4).

The Hillsborough requirement that there be clear evidence of congressional intent to preempt does not apply to every case where a statute has reserved power to the states. Hillsborough raises the standard for preemption when there is an attempt to preempt fundamental state regulation that preceded enactment of a federal statute. Inasmuch as the Court in MP&L, did not hold that the case involved preemption of pre-existing state regulation, Justice Scalia's concurrence in MP&L cannot be read as undermining Hillsborough. Further, even if MP&L had involved preemption of fundamental state regulation that preceded the FPA, TAPS' argument would still fail because Justices Brennan, Marshall and Blackman all differed with Justice Scalia on whether FERC's reading of limiting language warranted deference. Finally, Justice Stevens, writing for the majority, did not address this matter. TAPS' reliance on MP&L is misplaced.[3]

---

[3] TAPS' reference to FP&L is equally baseless. FP&L did not involve preemption. In the FPC's words, "[t]he only immediate effect of the Commission's order in this case will be to require FPL to follow the

B. FERC's Reversal of Position

As this Court held in Food and Drug Admin. v. Brown & Williamson Tobacco Corp., __ U.S. __, 120 S. Ct. 1291, 1312-1314 (2000), a federal agency's prior assurances to Congress are relevant to subsequent jurisdictional disputes. The States' petition points out that the D.C. Circuit's adoption of FERC's reading of FP&L, and its deference to FERC's reading of § 201, were further undermined by FERC's prior assurances to Congress that the elusive electron, or commingling, theory had no relevance to the states' regulation of retail matters (Pet. 14). In opposing certiorari, FERC does not deny (or even discuss) its previous insistence that commingling of electrons should have no bearing on the states' jurisdiction of retail services.[4] It argues, however, that its current position – that FP&L's recognition of commingling justifies federal preemption of retail transmission – should not invoke Food and Drug Admin. because FERC's new position was precipitated by unbundling and the advent of competition (FERC 14). Inconsistent statements to Congress (and the courts) are no less problematic when they are precipitated by alleged technological change. FERC's latest position directly conflicts with the assurances it provided Congress in opposing amendments to the FPA that would have preserved state jurisdiction over retail matters. The contradictions further establish why FERC's current position does not warrant deference. Watt v. Alaska, 451 U.S. 259, 273 (1981) ["the Department's current interpretation, being in conflict with its initial position, is entitled to considerably less deference"].

---

[4] Our petition confused a FERC decision and a Circuit Court decision when it described FPC Chairman White's 1967 testimony as following the Fifth Circuit's decision in FP&L (Pet. 14). The 1967 Congressional Hearings were held in response to the FPC's decision asserting authority over FP&L, 37 F.P.C. 544, decided March 20, 1967.

C. Section 212(h)

The State's petition establishes that Congress expressly preserved state authority over retail transmission in 1992 when it enacted FPA § 212(h) (Pet. 16). In response, FERC suggests that because § 212(h) "simply prohibits FERC from ordering transmission directly to an ultimate consumer" it does not support the States' position (FERC 15). Congress in 1992 (20 years after FP&L) would not have painstakingly safeguarded state regulation of retail transmission ["State law concerning the transmission of electric energy directly to an ultimate consumer" (§ 212(h))] if it had intended FERC to preempt state regulation of retail transmission.

D. The Retail/Wholesale "Bright Line"

The States' petition states that the D.C. Circuit's decision conflicts with the wholesale/retail "bright line" enunciated in FPC v. Southern Cal. Edison, 376 U.S. 205, 215 (1964) (Pet. 17). In response, FERC argues that Order 888 passes muster because the line only draws a distinction between transmission and distribution facilities (FERC 15-16). The bright line of FPC v. Southern Cal. Edison divides not transmission from distribution facilities, but retail services from wholesale services – with retail services being regulated by the states (L33-34). 376 U.S. at 214 [Congress adopted a test "which denied state power to regulate a sale 'at wholesale to local distributing companies' and allowed state regulation of a sale at 'local retail rates to ultimate consumers.'"].[5]

---

[5] Footnote 6 of Southern Cal. Edison (376 U.S. at 210 n.6) – cited by FERC as acknowledging the "absence of such a bright line" (FERC 16) – actually protected the retail/wholesale bright line by observing that the mere incidence of retail sales on low voltage wires used predominately to effectuate wholesale sales did not invoke § 201(b)'s local distribution exemption and prevent FERC from regulating all aspects of the wholesale sale, because FERC could rationally define the wires as wholesale transmission facilities.

E. Order 888's Impracticality

The State's petition observes that in directing that retail transmission rates for millions of customers throughout the nation will be set by FERC, Order 888 is not only impractical, but counterproductive to FERC's pro-competition policy (Pet. 18). In response, FERC quotes its own extra-record observation that many states have ordered retail unbundling "even after Order No. 888 ..." (FERC 17). What FERC does not address is where the states could have been if Order 888 had not pre-empted the states on retail transmission.

The D.C. Circuit's decision applied the wrong standard of judicial review; it misread FP&L; it ignored language limiting FERC's jurisdiction in §§ 201(a), 201(c) and 212(h); and it overstepped this Court's retail/wholesale bright line. The Court should grant review.

POINT II

FERC HAS FAILED TO JUSTIFY THE D.C. CIRCUIT'S AFFIRMANCE OF ITS PRE-EMPTION OF STATE REGULATION OF LOCAL DISTRIBUTION FACILITIES USED FOR WHOLESALE SALES.

The States' petition argues that the D.C. Circuit's affirmance of FERC preemption of wholesale local distribution regulation cannot be reconciled with § 201(b)(1) of the FPA, which denies FERC jurisdiction "over facilities ... used in local distribution" (States 19-21). The petition also notes that the D.C. Circuit failed to abide by CL&P, 324 U.S. 515, 531 (1944), wherein this Court held that § 201(b)(1)'s denial of jurisdiction was not conditioned on the type of electricity being carried by the utility (Pet. 20). Finally, the States assert that FERC's preemption of wholesale distribution facilities invites sham transactions (Pet. 21).

In response, FERC argues that § 201(b)'s jurisdictional limitations give way to § 201(a) which, in FERC's view, empowers FERC to regulate all aspects of wholesale sales (FERC 17). Further, FERC disputes that CL&P upholds state regulation of local distribution facilities that carry energy to recipients who resell it (FERC 17-18).

FERC's position is contrary to § 201(b), CL&P and this Court's teaching in FPC v. Southern Cal. Edison, 376 U.S. at 216, that FERC has jurisdiction over wholesale sales "except those reserved to states," such as local distribution (376 U.S. at 210 n.6). As noted above (n.5), n.6 of FPC v. Southern Cal. Edison, 376 U.S. at 210 n.6, observes that, assuming a rational basis, FERC may define low voltage wires as wholesale transmission facilities and thereby evade § 201(b)'s exemption, but it may not define the facilities as local distribution and preempt state regulation on a theory that the local distribution facilities are used for wholesale sales.[6]

As this Court noted in CL&P, § 201(b)'s denial of FPC jurisdiction "loomed importantly in the minds and speech of its sponsors, perhaps was necessary to get the bill passed, and is one which the Commission must observe and the courts must enforce." 324 U.S. at 529. The D.C. Circuit has not done so.[7]

---

[6] TAPS claims the states are trying to regulate wholesale sales on low voltage distribution systems (TAPS 5-6). The States' position is that the rule of law should be observed. Hence, if FERC defines systems as local distribution, it may not preempt state jurisdiction over such systems (Pet. 20-21).

[7] FERC suggests that there is no risk of sham transactions because Order 888 promises FERC will intervene on a case-by-case basis to avoid such wrongdoing. With all due respect, FERC's staff is hardly in a position to oversee rates for 2.5 million miles of distribution facilities. Further, the states should not be required to bring grievances to FERC over facilities that were expressly reserved to their jurisdiction by Congress.

POINT III

FERC AND ITS SUPPORTERS HAVE FAILED TO ANSWER THE STATES' DEMONSTRATION THAT THE D.C. CIRCUIT'S TREATMENT OF STRANDED COSTS WAS ERRONEOUS.

In affirming FERC's holding that, when state law denies rate recovery, FERC will sit in review of utility requests for recovery of costs stranded due to retail competition, the D.C. Circuit held that FERC's position did not impinge on state ratemaking (C81-C83). The States' petition shows that FERC's decision does, in fact, trivialize state retail rate decisions and is illogical because numerous factors, only one of which is open access, can cause (and are needed for) retail competition (Pet. 23).

In response, FERC contends that the fact that utility "stranded" costs were intended to serve retail customers is irrelevant because "rates are jurisdictional; costs are not" (FERC 20). FERC's assertion ignores Federal Power Commission v. Conway Corp., 426 U.S. 271, 278 (1976) [wherein the Court noted that wholesale rates, in order to be just and reasonable, should not include non-jurisdictional, retail sales].

FERC also attempts to downplay the significance of Order 888's intrusion into state ratemaking by contending that no state law has triggered the need for a FERC backstop (FERC 20). In the words of FPC Commissioner Seavey, when the FPA was enacted, "matters of a local nature ... should be handled locally and should receive the consideration of local men familiar with the local conditions in the communities involved." Hearings on H.R. 5423 at 393, quoted in Duke Power Co. v. Federal Power Commission, 401 F.2d, 930, 936 (D.C. Cir. 1968). The very existence of Order 888 limits the discretion of state legislators to resolve the rate treatment of costs incurred to serve retail customers, a particularly local matter.

In affirming FERC's directive that it would be the "primary forum" for deciding the rate treatment of utility costs incurred to serve retail customers, but "stranded" when a municipality decides to buy power from a utility competitor, the D.C. Circuit concluded that FERC was entitled to jurisdiction over such rate issues because its open access policy caused municipalization, which, in turn, caused retail costs to be stranded (C90). The States' petition pointed out, however, that an agency derives authority from its enabling legislation, not attenuated principles of causation (Pet. 24). See Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355, 374 (1986) ("[a]n agency literally has no power to act, let alone pre-empt the validly enacted legislation of a sovereign State, unless and until Congress confers power upon it .... An agency may not confer power upon itself.")

In reply, FERC quotes the D.C. Circuit's opinion and concludes, without explanation, that the D.C. Circuit was correct. If causation determines jurisdiction then, as FERC Commissioner Massey noted, it is state, not federal law, that allows municipalization (61 Fed. Reg. at 21736). As former FERC Chairman Hoecker emphasized, FERC's "primary forum" approach (1) requires FERC to second-guess state determinations on the rate treatment of retail costs; (2) encourages forum-shopping; and (3) is inconsistent with FERC's past practices on retail wheeling matters (61 Fed. Reg. at 21735-36).

CONCLUSION

The States' petition demonstrates that the D.C. Circuit decision affirming FERC Order 888 directly conflicts with numerous Supreme Court decisions and is inconsistent with the will of Congress. In their opposition to certiorari, FERC and its supporters fail to show otherwise. The Petitioners speak for 66 million citizens when they ask this Court to review the D.C. Circuit's decision.

Respectfully submitted,

Lawrence G. Malone
General Counsel
NYS Public Service Commission
3 Empire State Plaza
Albany, New York 12223-1350
(518) 474-2510

Jonathan D. Feinberg
Diane T. Dean
of Counsel

Dated: February 2, 2001
Albany, New York

JAMES BRADFORD RAMSAY
General Counsel
SHARLA M. BARKLIND
Assistant General Counsel
National Association of Regulatory Utility Commissioners
1101 Vermont Avenue, N.W.
Suite 200
Washington, D.C. 20044-0684
(202) 898-2208

CATHERINE BEDELL
General Counsel
RICHARD BELLAK
Associate General Counsel
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Fl 32399-0850
(850) 413-6092

ALAN G. LANCE
Attorney General
DONALD L. HOWELL, II
Deputy Attorney General
Idaho Public Utilities Commission
472 West Washington Street
P.O. Box 83720
Boise, ID 83720-0074
(208) 334-0312

JOHN J. FARMER, JR.
Attorney General
State of New Jersey
HELENE S. WALLENSTEIN
Sr. Deputy Attorney General
Attorney for New Jersey Board of Public Utilities
124 Halsey Street, 5th Floor
P.O. Box 45029
Newark, NJ 07101
(973) 648-4846

JOANNE SANFORD
North Carolina Utilities Commission
ROBERT P. GRUBER
Public Staff
North Carolina Utilities Commission
GISELE L. RANKIN
Staff Attorney
P.O. Box 29520
Raleigh, NC 27626-0520
(919) 733-2435

WILLIAM H. CHAMBLISS
General Counsel
C. MEADE BROWDER, JR.
Attorney Virginia State Corporation Commission
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218
(804) 371-9671

CHRISTINE O. GREGOIRE
Attorney General
WILLIAM BERGGREN COLLINS
Senior Assistant Attorney General
ROBERT D. CEDARBAUM
Senior Counsel for the Washington Utilities and Transportation Commission
P.O. Box 40128
Olympia, WA 98504-0128
(360) 664-1188

HARVEY L. REITER
for the Vermont Department of Public Service
MORRISON & HECKER
1150 18th Street, N.W.
Suite 800
Washington, D.C. 20036
(202) 785-9100

HARRY IVEY
for the Wyoming Public Service Commission
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002
(307) 777-7824

Supreme Court, U.S.
FILED
JUN 18 2001
CLERK

Nos. 00-568 AND 00-809

In The

Supreme Court of the United States

People of the State of New York and the Public Service Commission of the State of New York, et al.
Petitioners,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

Enron Power Marketing, Inc.,
Petitioner,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

JOINT APPENDIX (Vol. 1 of 2)

Louis R. Cohen *
Wilmer, Cutler & Pickering
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000
For Petitioner/Respondent, Enron Power Mkt., Inc.

Lawrence G. Malone *
Public Service Commission
of the State of New York
Three Empire State Plaza
Albany, NY 12223-1350
(518) 474-2510
For Petitioners, People of the State of New York, et al.

Theodore B. Olson *
Solicitor General
Edwin S. Kneedler
Deputy Solicitor General
Austin C. Schlick
Department of Justice
950 Pennsylvania Ave., N.W.
Room 5259
Washington, D.C. 20530-0001
(202) 514-2217
For Respondent, Federal Energy Regulatory Commission

* COUNSEL OF RECORD

BECKER GALLAGHER LEGAL PUBLISHING, INC.
CINCINNATI, OH 800-890-5001

James Bradford Ramsay
General Counsel
Sharla M. Barklind
Associate General Counsel
National Association of
Regulatory Utility Commissioners
1101 Vermont Ave., N.W., Ste. 200
Washington, D.C. 20005
(202) 898-2208

Catherine D. Bedell
General Counsel
Richard Bellak
Associate General Counsel
Florida Public Service
Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850
(850) 413-6092

Alan G. Lance
Attorney General
Donald L. Howell, II
Deputy Attorney General
Idaho Public Utilities
Commission
472 W. Washington Street
P.O. Box 83720
Boise, ID 83720-0074
(208) 334-0312

John J. Farmer, Jr.
Attorney General
State of New Jersey
Helene S. Wallenstein
Sr. Deputy Attorney General
Attorney for New Jersey Board
of Public Utilities
124 Halsey Street, 5th Floor
P.O. Box 45029
Newark, New Jersey 07101
(973) 648-4846

Counsel for Petitioners/Respondents
State Public Service Commissions

William H. Chambliss
General Counsel
C. Meade Browder, Jr.
Attorney
Virginia State Corp. Comm'n
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218
(804) 371-9671

Christine O. Gregoire
Attorney General
William Berggren Collins
Sr. Assistant Attorney General
Robert D. Cedarbaum, Sr. Counsel
(for the Washington Utilities and
Transportation Commission)
P.O. Box 40128
Olympia, WA 98504-0128
(360) 664-1188

Harvey L. Reiter
(for Vermont Dept. of Public Service)
Morrison & Hecker
1150 18th Street, N.W., Ste. 800
Washington, D.C. 20036
(202) 785-9100

Harry Ivey
(for Wyoming Public Service Comm'n)
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002
(307) 777-7824

Jo Anne Sanford
North Carolina Utilities Comm'n
Robert P. Gruber
Public Staff - North Carolina
Utilities Comm'n
Gisele L. Rankin, Staff Attorney
P.O. Box 29520
Raleigh, NC 27626-0520
(919) 733-2435

(Counsel continued on inside back cover)

TABLE OF CONTENTS

VOLUME I:

Relevant Docket Entries in District of Columbia Circuit . . . . . App. 5

Relevant Docket Entries Before Federal Energy Regulatory Commission . . . . . App. 15

Notice of Proposed Rulemaking - Recovery of Stranded Costs by Public Utilities and Transmitting Utilities in Docket No. RM 94-7-000, 59 Fed Reg. 35,274, 35,283-86; 7/11/94 . . . . . App. 17

Comments of North Carolina Utilities Commission and the Public Staff of the North Carolina Utilities Commission; pp. 1, 2-4, 6-7; 5/10/95 . . . . . App. 34

Order No. 888 Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities; pp. 31,632-31,684; 31,687-31,703; 31,718-31,736; 31,743-31,753; 31,764-31,766; 31,770-31,785; 31,898-31,899; 31,919-31,926; 31,966-31,981; 4/24/96 . . . . . App. 42

VOLUME II:

Part 35 - Filing of Rate Schedules - 61 Fed. Reg. 21692-21695; 5/10/96 . . . . . App. 431

Pennsylvania Public Utility Commission's Petition for Rehearing; pp. 1-2, 18-35; 5/23/96 . . . . . App. 444

Virginia State Corporation Commission's Request for Rehearing; pp. 1, 3-9; 5/24/96 . . . . . App. 467

Motion for Rehearing of the Public Service Commission of the State of New York; pp. 1-22; 5/24/96 . . . . . App. 475

Request of the National Association of Regulatory Utility Commissioners for Rehearing; pp. 1, 4-9; 5/24/96 . . . . . App. 499

Application of the Coalition for a Competitive Electric Market For Reconsideration and Clarification or, in the Alternative, Rehearing; pp. 1, 4-8; 5/24/96 . . . App. 509

Order No. 888-A - Order on Rehearing; pp. 30,172-30,188; 30,200-30,218; 30,255-30,226; 30,278-30,281; 30,334-30,350; 30,402-30,424; 30,503-30,543; 3/4/97 . . . . . App. 517

Brief for the Public Service Commissions of New York, Arkansas and Florida, et al.; pp. 1-20; 30-32; 8/19/99 . . . . . App. 792

Excerpts from Electric Power Flow Research Institute: *A Primer on Electric Power Flow for Economists and Utility Planners*; "Resistance and Ohm's Law" pp. 2-6 - 2-11; "Structures of Utility Systems" pp. 3-1 - 3-2; "Transmission and Distribution" pp. 3-12 - 3-17 . . . . . App. 818

NOTICE

The following documents have been omitted in the printing of this Appendix. These documents may be found in Petitioner Enron Power Marketing, Inc.'s Appendix to its Petition for Writ of Certiorari (00-809) at the following pages:

APPENDIX A:

Judgment of the United States Court of Appeals for the District of Colombia Circuit filed 6/30/00 . . . . . 1a

APPENDIX B:

Opinion of the United States Court of Appeals for the District of Columbia Circuit filed 6/30/00 . . . . . 3a

APPENDIX C:

Order of the United States Court of Appeals for the District of Columbia Circuit filed 8/22/00 . . . . . 123a

APPENDIX F:

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats, & Regs. ¶32,514 (1995) (pertinent portion) 33,047–33,085 . . . . . 553a

APPENDIX G:

Statutory Provisions 645a

APPENDIX H:

List of Parties to the Proceeding 683a

Some may also be found in the Petitioner's People of the State of New York and The Public Service Commission of the State of New York's Appendix to its Petition for Writ of Certiorari (00-568) at the following pages:

APPENDIX A:

Order of United States Court of Appeals for the District of Columbia Circuit filed 8/22/00 . . . . . A-1

APPENDIX B:

Judgment of United States Court of Appeals for the District of Columbia Circuit filed 6/30/00 . . . . . B-1

APPENDIX C:

Opinion of United States Court of Appeals for the District of Columbia Circuit decided 6/30/00 . . . . . C-1

APPENDIX G:

Statutory Provisions Involved G-1

RELEVANT DOCKET ENTRIES IN DISTRICT OF COLUMBIA CIRCUIT

DOCKET FOR CASE NOS.: 00-568 and 00-809
(Court of Appeals Docket No.: 97-1715, Complex)

12/5/97	PETITION FOR REVIEW CASE docketed. Petition for Review filed by Petition Transm Access Plcy. [314268-1] (mcm) [97-1715]
1/2/98	CLERK'S ORDER filed granting non-party motion to intervene filed by VT Dept Pub Srvc [316424-1]. (sha) [97-1715]
1/12/98	CLERK'S ORDER filed granting non-party motion to intervene filed by Edison Elec Inst [320723-1] granting non-party motion to intervene filed by City & Cty San [320823-1] granting non-party motion to intervene filed by Oprt Co Amer elec [318537-1]. (mcm) [97-1715]
4/30/98	CLERK'S ORDER filed, on court's own motion, that cases are consolidated; FURTHER ORDERED that EEI motion for leave to amend is granted. The amended motions are dismissed as moot, in light of 1/12/98 order granting EEI leave to intervene in 97-1715; FURTHER ORDERED that motions of WA Util, So CA Gas, KS City, PSI Energy, and Cincinnati Gas to intervene be granted; FURTHER ORDERED that parties advise the court by 5/15/98 of any remaining motions, etc.; FURTHER ORDERED that petitioners show cause, by 6/01/98 why the

petitions for review in 98-1110, 98-1117, 98-1121, 98-1130, 98-1133, 98-1135, 98-1138, 98-1144, 98-1151, 98-1157, 98-1158, 98-1161, 98-1164, 98-1167, 98-1179 should not be dismissed as incurably premature. Responses limited to 20 pages and failure to respond will result in dismissal. Respondent may file a reply, limited to 10 pages, within 10 days thereafter; FURTHER ORDERED that by 6/01/98, parties shall provide a list of five lead counsel. Within 30 days thereafter, counsel shall provide joint proposed briefing schedule, etc.; FURTHER ORDERED that parties shall resubmit Rule 26.1 disclosure statements by 6/01/98, etc.; FURTHER ORDERED that respondent shall provide by 5/15/98 a current master service list; Clerk is directed to send a copy of this order by certified mail to petitioners in cases identified above. (su) [97-1715 98-1179 98-1180]

6/2/98 CLERK'S ORDER filed granting non-party motion to intervene filed by Suffolk Cty Elec [355394-1] granting non-party motion to intervene filed by Fl Pub Svc Cmsn [354722-1] granting non-party to intervene filed by Rochester Gas & Elec [354086-1] granting non-party motion to intervene filed by Carolina Power [353289-1] granting non-party motion to intervene filed by FL Power & Light [353301-1] granting non-party motion to intervene filed by Pub Svc Elec Gas [353314-1] granting non-party motion to intervene filed by OH Consum Coun, Natl Assn St Util [353328-1] granting non-party motion to

intervene filed by Dairyland Power Coop [353189-1] granting non-party motion to intervene filed by Natl Rural Elec Coop [353333-1] granting non-party motion to intervene filed by NE TX Elec Coop Inc, Sam Rayburn Elec G&T, TX-LA Elec Coop TX [352000-1] granting non-party motion to intervene filed by FL Muni Power Agcy [352033-1] granting non-party motion to intervene filed by MI S Ctrl Power Agcy [352034-1] granting non-party motion to intervene filed by Wolverine Power [352035-1] granting non-party motion to intervene filed by Pub Svc Cmsn St NY [352047-1] granting non-party motion to intervene filed by Natl Assn Reg Util [352050-1] granting non-party motion to intervene filed by NY St Elec & Gas [350758-1] granting non-party motion to intervene filed by GA Transm Corp [354045-1]. (mcm) [97-1715]

8/13/98 PER CURIAM ORDER: on the court's own motion, that these case be designated "COMPLEX". FURTHER ORDERED that the order to show cause be discharged. FURTHER ORDERED that the petitions for review in No. 98-1110, 98-1117, 98-1121, 98-1130, 98-1133, 98-1135, 98-1138, 98-1144, 98-1151, 98-1157, 98-1161, 98-1167 and 98-1179 be dismissed as incurably premature. [374127-1] FURTHER ORDERED that the initial briefing schedule is as follows (SEE ORDER FOR BRIEFING FORMATS) [374127-2]: Petitioner's brief due on 10/1/98 in 97-1715; Intervenor supprtng Petitioner's

brief due 10/1/98 in 97-1715; Respondent's brief due on 2/1/99 in 97-1715; Intervenor supportg Respondent's brief due 4/1/99 in 97-1715; Petitioner's reply brief due 5/3/99 in 97-1715; Intervenor supprt Petitioner's reply brief due 5/3/99 in 97-1715; Deferred appendix due on 6/10/99 in 97-1715; Final briefs due on 6/24/99 in 97-1715. FURTHER ORDERED that motion for leave to file joint proposed briefing schedule be granted. The Clerk is directed to file the lodged pleading [363672-1]. FURTHER ORDERED that the motion to exceed page limits be granted. FURTHER ORDERED that the motion to change party name be granted. The Clerk is directed to amend the docket to reflect that the intervenor's name is Enron Power Marketing, Inc. rather than the Coalition for a Competitive Elec Market [360864-1]. FURTHER ORDERED that the motion to intervene filed by IL Power Co [360901-1] be granted. FURTHER ORDERED that the motions adding a new attorney [356458-1] filed by 11 movants and Ontario Hydro [356721-1] be granted. Lead counsel are as follows: John Conway (FERC), Susan Court (FERC), Robert Zener, Robert Jablon, Jonathan Feinberg, Sara Schotland, Peter Kirby and Isaac Benkin (lead counsel for petitioners and intervenors). FURTHER ORDERED that the motion of Pacific Legal Fndtn for leave to participate as amicus [353194-1] and for leave to dispense with service on all parties be denied [353194-2]. This denial is without prejudice to PLF's refiling the motion for

leave within ten days of the date of this order, after serving all parties listed in the current master list. Before Judges Wald, Sentelle, Randolph. [97-1715] (mcm) [97-1715 98-1110 98-1117 98-1121 98-1130 98-1133 98-1135 98-1138 98-1144 98-1151 98-1157 98-1161 98-1167 98-1179]

8/13/98 PER ABOVE ORDER lodged motion establishing the initial briefing schedule [363672-1] is filed. (mcm) [97-1615]

10/1/98 BRIEF [DISCRIMINATORY DISCOUNTING AND FUNCTIONAL UNBUNDLING] filed by Petitioner Transm Access Plcy in 97-1715, Petitioner Transm Dpndnt Util in 98-1145, Petitioner Enron Power Mkt Inc in 98-1178 [386444-1]. Copies: 15. of service date 10/1/98. [97-1715, 98-1145, 98-1178] (mcm) [97-1715 98-1145 98-1178]

10/1/98 BRIEF [INVESTOR OWNED UTILITY PETITIONERS] filed by Investor IL Power Co in 97-1715, Petitioner Pub Svc Elec & Gas in 98-1119, Petitioner FL Power & Light in 98-1120, Petitioner Rochester Gas & Elec in 98-1124, Petitioner Carolina Power in 98-1125, Petitioner NE Util Svc Co in 98-1126, Petitioner NE Util Svc Co in 98-1127, Petitioner NY St Elec & Gas in 98-1139, Petitioner Boston Edison Co in 98-1162, Petitioner Ctrl VT Pub Svc Corp in 98-1162, Petitioner Niagra Mohawk Power in 98-1168, Petitioner Con Edison Co NY Inc in 98-1174,

Petitioner Con Edison Co NY Inc in 98-1175, Petitioner GPU Engy in 98-1176, Petitioner Edison Elec Inst in 98-1180 [386545-1]. Copies: 7. Certificate of service date 10/1/98. [97-1715, 98-1119, 98-1120, 98-1124, 98-1125, 98-1126, 98-1127, 98-1139, 98-1162, 98-1168, 98-1174, 97-1175, 98-1176, 98-1180] (mcm) [97-1715 98-1119 98-1120 98-1124 98-1125 98-1126 98-1127 98-1139 98-1162 98-1168 98-1174 98-1175 98-1176 98-1180]

10/2/98 BRIEF W/2 VOLUME APPENDIX OF LEGESLATIVE HISTORY [STATE COMMISSIONS] filed by Intervenor for Petitioner WA Util Trans Cmsn in 97-1715, Intervenor St NJ Bd Pub Util in 97-1715, Intervenor WY Pub Svc Cmsn in 97-1715, Intervenor for Petitioner ID Pub Util Cmsn in 97-1715, Intervenor for Petitioner NC Util Cmsn in 97-1715, Intervenor for Petitioner Natl Assn Reg Util in 97-1715, Intervenor for Petitioner FL Pub Svc Cmsn in 97-1715, Petitioner People St NY in 98-1111, Petitioner Pub Scv Cmsn St NY in 98-1111, Petitioner VA St Corp Cmsn in 98-1142, Petitioner AR Pub Svc Cmsn in Petitioner VT Dept Pub Srvc in 98-1148, Petitioner OH Coun in 98-1150, Petitioner Natl Assn St Util in 98-1155 [386734-1]. Copies: 7. Certificate of service date 10/1/98. [97-1715, 98-111, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155] (mcm) [97-1715 97-1111 98-1142 98-1147 98-1148 98-1150 98-1155]

2/16/99 BRIEF filed by Respondent FERC in 97-1715 [416562-1]. Copies: 6. Certificate of service date 2/16/99. (mcm) [97-1715]

4/16/99 BRIEF filed by Intervenor Edison Elec Inst in 97-1715, Intervenor NY St Elec & Gas in 97-1715, Intervenor Cm Edison Co in 97-1715, Intervenor Consum Engy Co in 97-1715, Intervenor VA Elec Power Co in 97-1715, Intervenor New Engl Power Co in 97-1715, Intervenor WI Pub Svc Corp in 97-1715, Intervenor Atl City Elec Co in 97-1715, Intervenor for Repsondent FL Power & Light in 97-1715, Intervenor Rochester Gas & Elec in 97-1715; Intervenor FL Power Corp in 97-1715 [430200-1]. Copies: 6. Certificate of service date 4/16/99. (mcm) [97-1715]

5/18/99 REPLY BRIEF [DISCRIMINATORY DISCOUNTING AND FUNCTIONAL UNBUNDLING] filed by Petitioner Transm Access Plcy in 97-1715, Petitioner Transm Dpndnt Util in 98-1145, Petitioner Enron Power Mkt Inc in 98-1178 [436794-1]. Copies: 7. Certificate of service date 5/18/99. [97-1715, 98-1145, 98-1178] (mcm) [97-1715 98-1145 98-1178]

5/19/99 REPLY BRIEF [STATE COMMISSIONS] filed by Intervenor for Petitioner WA Util Trans Cmsn in 97-1715, Intervenor St NJ Bd Pub Util in 97-1715, Intervenor WY Pub Svc Cmsn in 97-1715, Intervenor for Petitioner Pub Stf NC Util Cmsn in 97-1715, Intervenor for Petitioner NC Util Cmsn in 97-1715,

Intervenor for Petitioner Natl Assn Reg Util in 97-1715, Intervenor FL Pub Svc in 97-1715,k Petitioner People St NY in 98-1111, Petitioner Pub Svc Cmsn St NY in 98-1111, Petitioner VA St Corp Cmsn in 98-1142, Petitioner VT Dept Pub Srvc in 98-1148, Petitioner OH Consum Coun in 98-1150, Petitioner Natl Assn St Util in 98-1155 [436812-1]. Copies: 7. Certificate of service date 5/18/99. [97-1715, 98-1111, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155] (mcm) [97-1715 98-1111 98-1142 98-1147 98-1148 98-1150 98-1155]

8/19/99 FINAL BRIEF filed by Intervenors for Respondent, Enron Power Marketing, Inc., Electricity Consumers Resource Council, American Public Power Association, NE TX Elec Coop Inc, Sam Rayburn Elec G&T, Tex-La Elec Coop TX, Natl Rural Electric Cooperative Assoc., et al. in 97-1715 [458098-1]. Copies: 15. Certificate of service date 8/19/99. [STYLED AS JOINT BRIEF FOR ALL OTHER INTERVENORS IN SUPPORT OF RESPONDENT]. (lvs) [97-1715]

8/19/99 FINAL BRIEF filed by Petitioners Transm Access Plcy, Transm Dpndnt Util, Enron Power Mkt Inc [488131-1]. Copies: 15. Certificate of service date 8/19/99. [STYLED AS INITIAL BRIEF OF THE TRANSMISSION ACCESS POLICY STUDY GROUP, ENRON POWER MARKETING, INC. AND TRANSMISSION DEPENDENT UTILITY SYSTEMS ON FUNCTIONAL UNBUNDLING AND DISCOUNTING]. [97-

1715, 98-1145, 98-1178] (lvs) [97-1715 98-1145 98-1178]

8/19/99 FINAL REPLY BRIEF filed by Petitioners Transm Access Plcy, Transm Dpndnt Util, Enron Power Mkt Inc [458144-1]. Copies: 15. Certificate of service date 8/19/99. [STYLED AS REPLY BRIEF OF THE TRANSMISSION ACCESS POLICY STUDY GROUP, ENRON POWER MARKETING, INC. AND TRANSMISSION DEPENDENT UTILITY SYSTEMS ON FUNCTIONAL UNBUNDLING AND DISCOUNTING]. [97-1715, 98-1145, 98-1178] (lvs) [97-1715 98-1145 98-1178]

8/20/99 FINAL BRIEF for the Public Service Commissions of New York, Arkansas and Florida, ID Pub Util Cmsn, NC Util Cmsn, WY Pub Svc Cmsn, NJ Board of Public, VA Corp Cmsn, WA Util Trans Cmsn, VT Dept Pub Srvc, Natl Assn Reg Util [458523-1]. Copies: 15. Certificate of service date 8/19/99. [97-1715, 98-1142, 98-1147, 98-1148, 98-1162, 98-1169] (lvs) [97-1715 98-1142 98-1147 98-1148 98-1162 98-1169]

8/20/99 FINAL REPLY BRIEF filed by Petitioners/Intervenors VA St Public Service Commissions of NY, AR and FL, Natl Assn of Regulatory Util Cmsn, Pub Util Cmsn ID, NC and WY, NJ Board Pub Util, VA Corp Cmsn, WA Util Trans Cmsn, VT Dept Pub Srvc, OH Consum Coun, Natl Assn St Util [458643-1]. Copies: 15. Certificate of service

date 8/19/99. [97-1715, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155, 98-1162, 98-1169] (lvs) [97-1715 98-1142 98-1147 98-1148 98-1150 98-1155 98-1162 98-1169]

8/20/99 APPENDIX [VOLUME I & II] OF LEGISLATIVE HISTORY FOR STATE COMMISSIONS' BRIEF filed by Petitioners/Intervenors Pub Svc Cmsn NY, AR, FL, Natl Assn of Regulatory Util Cmsn, Pub Util Cmsn ID, NC and WY, NJ Board Pub Util, VA Corp Cmsn, WA Util/Trans Cmsn, VT Dept Pub Srvc, OH Consum Coun [458663-1]. Copies: 10. Certificate of service date 8/19/99. [97-1715, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155, 98-1162, 98-1169] (lvs) [97-1715 98-1142 98-1147 98-1148 98-1150 98-1155 98-1162 98-1169]

RELEVANT DOCKET ENTRIES BEFORE FEDERAL ENERGY REGULATORY COMMISSION

Issuance 19980421-0175	3/4/97	Ltr to Vice President A Gore, Jr providing final rules issued on promoting wholesale competition through open access non-discriminatory transmission servs by public utils etc under RM95-8 et al. Portland General Elec Co submits.
Submittal 19960530-0195	5/24/96	Motion for rehearing of Public Serv Commission of New York of Order 888 & 889 re open access transmission & stranded costs under RM95-8 & RM94-7.
Submittal 19960530-0202	5/24/96	Pennsylvania Public Util Commission member J Hanger submits ltr of dissent re 960523 petition for rehearing of Order 888 under RM95-8 & RM94-7.
Submittal	5/24/96	Appl of Coalition for

19960530-0279		Competitive Elec Market for reconsideration & clarification or in alternative rehearing of FERC's Order 888 re promoting wholesale competition etc.
Submittal 19960530-0188	5/23/96-5/24/96	Request of Virginia State Corp Commission for rehearing of Order 888 re open access transmission etc under RM94-7 & RM95-8.
Issuance 19960425-0263	4/24/96	Order 888 final rule re promoting wholesale competition thru open access nondiscriminatory svc/recovery of stranded costs by public utils. Corrected Hoecker.
Submittal 19950811-0061	8/7/95-8/10/95	Comments of NC Utilities Commission re notice of proposed rulemaking & suppl notice of proposed rulemaking re recovery of stranded cost by public utilities etc under RM95-8, et al.

NOTICE OF PROPOSED RULEMAKING - RECOVERY OF STRANDED COSTS BY PUBLIC UTILITIES AND TRANSMITTING UTILITIES IN DOCKET NO. RM-94-7-000
59 FED. REG. 35,274; 35,283-86

[pp. 35,274; 35,283-86]

[35,274]

SUMMARY: The Commission is proposing to amend its regulations to establish provisions concerning the recovery of wholesale and retail stranded costs by public utilities and transmitting utilities under sections 205, 206, 211 and 212 of the Federal Power Act. The Commission seeks public comment concerning the issues raised by the proposed rulemaking.

DATES: Written comments must be received by the Commission by September 9, 1994. Reply comments must be received by the Commission by October 11, 1994.

ADDRESSES: Send comments to: Office of the Secretary, Federal Energy Regulatory Commission, 825 North Capitol Street, NE., Washington, DC 20426.

FOR FURTHER INFORMATION CONTACT:

James H. Douglass, Office of the General Counsel, Federal Energy Regulatory Commission, 825 North Capitol Street, NE., Washington, DC 20426; Telephone: (202) 208-2143 (legal issues).

Michael A. Coleman, Office of Electric Power Regulation, Federal Energy Regulatory Commission, 825 North Capitol

Street, NE., Washington, DC 20426; Telephone: (202) 208-1236 (technical issues).

SUPPLEMENTARY INFORMATION: In addition to publishing the full text of this document in the **Federal Register**, the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in room 3104, at 941 North Capitol Street, NE., Washington, DC 20426.

The Commission Issuance Posting System (CIPS), an electronic bulletin board service, provides access to the texts of formal documents issued by the Commission. CIPS is available at no charge to the user and may be accessed using a personal computer with a modem by dialing (202) 208-1397. To access CIPS, set your communications software to use 300, 1200, or 2400 bps, full duplex, no parity, 8 data bits and 1 stop bit. CIPS can also be accessed at 9600 bps by dialing (202) 208-1781. The full text of this order will be available on CIPS for 30 days from the date of issuance. The complete text on diskette in WordPerfect format may also be purchased from the Commission's copy contractor, La Dorn Systems Corporation, also located in room 3104, 941 North Capitol Street, NE., Washington, DC 20426.

Notice of Proposed Rulemaking

June 29, 1994.

Table of Contents

I. *Introduction*
II. *Public Reporting Burden*

III. *Discussion*
A. Background
B. Current Stranded Cost Policy
1. *Wholesale Customers Leaving The System*
2. *Retail-Turned-Wholesale Customers Leaving The System*
3. *Retail Customers Leaving The System*
C. The Proposed Regulations
1. *Recovery of Stranded Costs Associated With New Wholesale Power Sales Contracts*
2. *Recovery of Stranded Costs Associated With Existing Wholesale Power Sales Contracts*
3. *Recovery Of Wholesale Stranded Costs In Wholesale Transmission Rates*
4. *Filing Requirements For Wholesale Stranded Cost Recovery*
5. *Evidentiary Demonstration For Wholesale Stranded Cost Recovery*
6. *Recovery Of Retail Stranded Costs*
i. *Jurisdictional Analysis*
ii. *Treatment of Retail Costs*
IV. *Regulatory Flexibility Act*
V. *Environmental Statement*
VI. *Information Collection Statement*
VII. *Public Comment Procedures*
Regulatory Text

I. Introduction

The Federal Energy Regulatory Commission (Commission) seeks public comment on amending its regulations to establish provisions concerning the recovery of wholesale and retail stranded costs by public utilities and

transmitting utilities under sections 205, 206, 211 and 212 of the Federal Power Act (FPA).[1] Wholesale stranded costs are defined as any legitimate, prudent and verifiable costs incurred by a public utility or a transmitting utility to provide service to a wholesale requirements customer that subsequently becomes, in whole or in part, an unbundled transmission services customer[2] of that public utility or transmitting utility. Retail stranded . . .

[35283]

---

[1]A public utility is defined under section 201(e) of the FPA as "any person who owns or operates facilities subject to the jurisdiction of the Commission under this Part (other than facilities subject to such jurisdiction solely by reason of section 210, 211, or 212)." A transmitting utility is defined under section 3(23) of the FPA as "any electric utility, qualifying cogeneration facility, qualifying small power production facility, or Federal power marketing agency which owns or operates electric power transmission facilities which are used for the sale of electric energy at wholesale." Not all transmitting utilities are public utilities. For instance, a municipally-owned electric utility that owns transmission facilities which are used for the sale of electric energy at wholesale is a transmitting utility, but is not a public utility.

[2]An unbundled transmission services customer is one who purchases transmission as a product that is separate from the purchase of generation.

6. Recovery of Retail Stranded Costs

As discussed earlier, there are two general ways in which retail stranded costs are likely to occur:[50] (1) A retail franchise customer may, through State or local government action, become a wholesale customer who can then obtain unbundled transmission services in order to reach a new power supplier;[51] (2) a retail franchise customer may obtain voluntary unbundled retail transmission services from its existing power supplier in order to reach a new power supplier, or there may be a State or local action that results in the existing supplier **[35,281]** providing such retail transmission services.

In the first example (a retail franchise customer becomes an unbundled wholesale power and transmission customer), the Commission clearly has exclusive jurisdiction under sections 201, 205 and 206, or section 212 of the FPA, over the rate for the wholesale interstate transmission services[52] used by the new wholesale entity in order to reach its new generation supplier. In the second example, in which

---

[50]Retail stranded costs may result from "self-help" actions such as customer self-generation, and this has long been a fact of life for utilities. *See, supra*, n.18. This proceeding does not address these situations.

[51]In addition, certain retail customers may become retail customers of a newly-created wholesale entity.

[52]Under FPA section 211, the Commission's authority to order wheeling does not turn on whether the transmission services will be in interstate commerce.

a retail franchise customer becomes a retail unbundled transmission customer of its former franchise utility, and a retail power customer of another utility, we conclude that we also have exclusive jurisdiction over the rates, terms and conditions for the retail interstate transmission services.[53]

(i) Jurisdictional Analysis

The Commission's jurisdiction over the rates, terms and conditions of transmission in interstate commerce derives from Congress' power to regulate interstate commerce under the United States Constitution[54] and the FPA. When Congress enacted the FPA, it gave the Commission exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. The Supremacy Clause of the Constitution provides that federal laws enacted pursuant to the powers delegated to the federal government by the United States Constitution are the supreme law of the land.[55] Accordingly, to the extent that retail wheeling involves transmission in interstate commerce by public utilities, the rates, terms and conditions of such service

---

[53]We make no determination here regarding the physical or jurisdictional distinctions between transmission and local distribution. Section 201(b)(1) of the FPA states that the Commission has no jurisdiction, except as specifically provided in Parts II and III of the FPA, over facilities used for local distribution. Nor do we address here whether States have authority to order retail wheeling in interstate commerce.

[54]U.S. Const. Art. I, § 8, cl.3.

[55]U.S. Const. Art. VI, cl.2.

are subject to the exclusive jurisdiction of the Commission, and the rates for such service must be filed with the Commission.[56]

Section 201 of the FPA, by its very words, does not limit the Commission's jurisdiction over transmission to transmission of electric energy in interstate commerce sold at wholesale.

Subsection 201(b)(1) of the FPA provides:

(b)(1) The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce * * * The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy * * *

16 U.S.C. § 824(b)(1).

Much of the legislative history of the FPA indicates that Congress intended the Commission's jurisdiction to extend only to those matters which the *Attleboro* decision[57] held to be beyond the reach of the States. For instance, the

---

[56]*See* Montana-Dakota Utilities Co. v. Northwestern Public Service Co., 341 U.S. 246, 251-52 (1951) (*Montana-Dakota*).

[57]Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927) (*Attleboro*). In *Attleboro*, the Supreme Court held that State regulation of the interstate sale of electricity was barred by the Commerce Clause because such regulation would impose a "direct burden" on interstate commerce.

report accompanying the Senate bill states that subsection (b) "leaves to the States the authority to fix local rates even in cases where the energy is brought in from another state."[58] The Senate report also states:

> The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in [*Attleboro*] to be beyond the reach of the States. Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines. * * *

S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). Thus, federal jurisdiction over transmission lines is not dependent on whether those lines are used to effect a sale, wholesale or otherwise.

While the provisions of section 201 reserving certain regulatory authority to the States have been interpreted narrowly,[59] the courts have construed "in interstate commerce" broadly. The term does not turn on whether the

---

[58]S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). *See also* H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935).

[59]While Congress may exercise its Commerce Clause authority to grant the States that "ability to restrict the flow of interstate commerce that they would not otherwise enjoy," Lewis v. BT Investment Managers, Inc., 447 U.S. 27, 44 (1980), States may not exercise such regulatory powers unless Congress has expressly stated its intention to make such an affirmative grant of power. New England Power Co. v. New Hampshire, 55 U.S. 331, 343 (1982).

contract path for a particular power or transmission sale crosses state lines, but rather follows the physical flow of electricity. Because of the highly integrated nature of the electric system, this results in most transmission of electric energy being "in interstate commerce.

For example, in *Jersey Central Power & Light Co. v. FPC*, 319 U.S. 61 (1943), the Court stated:

> It is impossible for us to conclude that this definition [of transmission in interstate commerce] means less than it says and applies only to the energy at the instant it crosses the state line and so only to the facilities which cross the line and only to the company which owns the facilities that cross the line.

319 U.S. at 71. Thus, a critical question regarding the jurisdictional status of a wheeling transaction is whether the facilities used to provide the service transmit electric energy in interstate commerce. *See also Connecticut Light & Power Co. v. FPC*, 324 U.S. 515 (1945) (CL&P); *FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972). In *CL&P*, the Court emphasized that whether certain facilities transmit electric energy in interstate commerce is more a technical than a legal question. The Court stated, "[f]ederal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test." 324 U.S. at 529.

In all of the above cases, the Court's decisions turned on whether energy flowed in interstate commerce as a technical matter. The decisions did not turn on whether the energy flowing in interstate commerce was being sold for

resale or was being sold to an end user. However, under FPA section 201(b), the Commission does not have jurisdiction over facilities used in local distribution. In *CL&P*, the Court stated that local distribution facilities are exempt from Commission jurisdiction even if those facilities "carry no energy except extra-state energy." 324 U.S. at 531. The Court rejected the argument that transmission and local distribution facilities could be distinguished by the proportion or amount of interstate energy that they carried:

> We do not find that Congress has conditioned the jurisdiction of the Commission upon any particular volume or proportion of interstate energy involved, and we do not think it would be appropriate to supply such a jurisdictional limitation by construction.

324 U.S. at 536. The determination of whether facilities are local distribution facilities remains a factual matter to be decided in the first instance by the Commission. *See FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964).

While the precise demarcation between transmission and local distribution remains unclear, and the Commission has not yet definitively addressed this issue, there is nothing in the statute, its legislative history, or the case law to indicate that the Commission's jurisdiction over rates, terms and conditions of transmission in interstate commerce extends only to **[35,285]** wholesale transmission and not retail transmission.

(ii) Treatment of Retail Costs

Because the Commission has jurisdiction over the rates, terms and conditions of both wholesale and retail transmission services in interstate commerce by public utilities, arguably it may allow retail stranded cost recovery in rates for either wholesale or retail transmission services. There nevertheless may be important legal or policy reasons to exclude retail stranded costs from transmission rates. As noted earlier, however, the Commission has been presented only with the question of whether it should permit public utilities to seek recovery in *wholesale* transmission rates of stranded investment costs incurred to serve former retail customers (Scenario 2, section III.A.). The Commission has not been presented with the question of whether it should permit public utilities to seek recovery in *retail* transmission rates of stranded costs incurred to serve the customer when it was a retail customer (Scenario 3, section III.A.).

While we believe the Commission has the authority to address retail stranded costs through its jurisdiction over the rates, terms and conditions of interstate transmission services used by retail or newly-created wholesale customers, we also believe that the recovery of the costs of transition to competition at the retail level is a matter that should be addressed by State authorities. This is because retail stranded costs will occur primarily as a result of State and local decisionmaking regarding retail franchise areas and the creation of new wholesale entities. In particular, the Commission believes it is incumbent upon states to deal with the consequences of stranded costs that occur as a result of retail wheeling. Our strong policy preference is that states explicitly address the issue. State and local decisionmakers

have a first-hand understanding of the regulatory bargain with respect to stranded costs incurred to serve retail customers, and they are familiar with the planning, investment and purchase activities of the utilities they regulate.

There are a number of procedural mechanisms which we believe States can use to address retail stranded costs. For example, a State that permits a retail franchise customer to become a wholesale entity may consider whether to impose an exit fee prior to, or as a condition of, creating the wholesale entity. Similarly, a State may consider whether to require payment of an exit fee prior to a franchise customer being permitted to obtain unbundled retail wheeling. In situations in which local distribution facilities are used by a retail wheeling customer, the State may consider whether to allow recovery of stranded costs through rates for local distribution services. If a State decides not to impose exit fees, or a surcharge through distribution rates, it may consider whether to allow recovery of stranded costs from remaining customers.

In situations in which a new wholesale entity obtains ownership or control of a franchise utility's transmission or distribution facilities, it is possible that State condemnation proceedings will provide a forum for a utility to seek recovery of any stranded costs. *What types of payments, if any, do new municipal utilities make to prior service providers? Do these reimbursements allow for recovery of stranded generation costs? Is there variation among the States as to the legal ability of local entities to municipalize? Is there variation among the States as to the payments made by new municipal utilities to previous suppliers?*

There may, of course, be other mechanisms which States can use to determine whether to allow stranded cost recovery, and from whom to allow recovery. *The Commission solicits comments on what other mechanisms might be used, and whether these mechanisms are adequate to deal with retail stranded costs.*

While our strong preference is for States to address retail stranded costs in whatever way they deem appropriate, we are willing to explore whether there are circumstances under which this Commission should consider claims for recovery of retail stranded costs. *We will therefore present two proposed alternatives regarding retail stranded costs, and seek comment on both.* However, as noted above, we express no preference in favor of either alternative.

Under the first alternative, the proposed rule provides that if in a specific circumstance an appropriate State authority explicitly considers and deals with retail stranded costs and there is no conflict within or among State regulatory bodies regarding a State's disposition of the issue, this Commission will not entertain a request for retail stranded cost recovery. However, in the absence of a clear expression by an appropriate State authority that it has dealt with the issue, or in the event of a conflict between States[60] or among State

---

[60]For example, a conflict between States could result if State A's legislature allows a former retail customer to become a wholesale entity and the wholesale entity obtains transmission services so that it now takes only one half of its 100 MW load from its current utility supplier, which is a multistate utility. As a result of State A's action, the utility has retail stranded costs for 50 MW of generation. State A's commission allocates the utility's retail

officials within a single state, the Commission proposes to entertain requests to recover retail stranded costs.

Under the second alternative, the proposed rule provides that the Commission will not entertain any request for recovery of retail stranded costs. Under this proposal, State or local authorities will be the only forum for addressing the issue. The aforementioned preference for States to address retail stranded costs in whatever way they deem appropriate, the need for regulatory certainty, and the States' knowledge and expertise regarding utility planning, investment and purchase activities arguably favors the second alterative. *However, we solicit comment on whether there should be limited exceptions to the second alternative rule.*

As to both alternatives, the Commission solicits comments on the following questions.

Are there circumstances under which it is not necessarily appropriate to defer to the States (e.g., where one State takes an action regarding retail stranded costs which has adverse consequences for another State)? Are there circumstances under which a State may not have an adequate mechanism for addressing retail stranded costs, and may want the Commission to provide a forum?

---

costs so that State A's retail customers are responsible for only one half of the stranded costs. State B's commission, the other State in which the utility operates, allocates the utility's retail costs so that none of the retail stranded costs are allocated to State B's retail customers.

If a State does not explicitly address stranded costs resulting from an action that allows retail customers to purchase from a supplier other than the franchised utility, should this Commission entertain requests from the utilities left with the stranded costs? Beyond silence from the State, are there other factors that the Commission should consider before accepting requests for retail stranded cost recovery? Specifically, would financial health and possible adverse impacts on reliability be sufficient reason for Federal action?

The Commission further solicits comments on the following questions:

(1) Does the Commission have legal authority to allow retail stranded costs in rates for wholesale transmission services? Should the Commission do so as a matter of policy? If so, which costs?

(2) Does the Commission have legal authority to allow retail stranded costs **[35,286]** *in rates for retail transmission service? Should the Commission do so as a matter of policy? If so, which costs?*

(3) Does FPA section 212 give the Commission legal authority to allow recovery of retail stranded costs in rates for wholesale transmission services under FPA section 211?

(4) Are there legal or policy reasons why in Scenario 2 (p. 15), the Commission should entertain requests for recovery of retail stranded costs in wholesale transmission rates, but should not entertain requests for recovery of retail stranded costs in retail transmission rates in Scenario 3 (section III.A.)?

If the Commission determines that it will entertain requests for recovery of retail stranded costs through rates for wholesale or retail transmission in interstate commerce, the Commission proposes not to apply the "reasonable expectation" test used for wholesale stranded costs. To apply such a test would require a hearing on whether the franchise utility had a reasonable expectation, *e.g.*, of having its franchise renewed, of municipalization occurring, or of a section 212(h) non-sham wholesale entity being created by the State or local authority. No such test appears warranted because, in general, there is at the retail level an obligation to serve which is much stronger than any contractual obligation to serve at the wholesale level. The regulatory compact that has governed provision of retail service includes an implicit obligation to purchase concomitant with the utility's obligation to serve.

The Commission requests comments on whether these assumptions are correct, i.e., is the reasonable expectation test inapplicable to retail stranded costs? Are there situations, for instance, in which utilities could have expected municipalization to occur based on an established course of dealing?

Based on these assumptions, if the Commission determines that it will entertain requests for retail stranded costs, the proposed regulations for retail stranded costs would require only a showing of the dollar amounts that have been stranded as a result of the retail customer no longer taking bundled service from the franchise utility's system. In essence, this results in direct assignment of retail stranded costs to the former franchise customer. *The Commission requests comments on how to determine retail stranded costs*

as a general matter. Is there a future time when a retail customer's action of leaving a local franchise no longer has any adverse economic consequences on the franchise utility? If so, what is an appropriate way to make such a determination?

[pp. 1-4]

Comments of North Carolina Utilities Commission and the Public Staff of the North Carolina Utilities Commission

Designated Pages - 1-4, 6-7

[2]

COMMENTS OF THE
NORTH CAROLINA UTILITIES COMMISSION
AND THE
PUBLIC STAFF - NORTH CAROLINA UTILITIES COMMISSION

TO THE

FEDERAL ENERGY REGULATORY COMMISSION

REGARDING

NOTICE OF PROPOSED RULEMAKING AND
SUPPLEMENTAL
NOTICE OF PROPOSED RULEMAKING

DOCKET NO. RM95-8-000
PROMOTING WHOLESALE COMPETITION
THROUGH OPEN ACCESS NON-DISCRIMINATORY
TRANSMISSION SERVICES BY PUBLIC UTILITIES

DOCKET NO. RM94-7-00 1
RECOVERY OF STRANDED COSTS BY
PUBLIC UTILITIES AND TRANSMITTING UTILITIES

[3]

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

[Filed August 10, 1995]

Docket Nos. RM95-8-000 and RM94-7-001

Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities	)
Recovery of Stranded Costs by Public Utilities and Transmitting Utilities	)

INITIAL COMMENTS OF THE NORTH CAROLINA UTILITIES COMMISSION AND THE PUBLIC STAFF-NORTH CAROLINA UTILITIES COMMISSION

The North Carolina Utilities Commission (NCUC) and the Public Staff of the North carolina Utilities Commission (Public Staff) respectfully offer the following comments for consideration by the Federal Energy Regulatory Commission (FERC) in its proposed rulemaking in Docket Nos. RM95-8-000 and RM94-7-001 regarding open access to the electric transmission system and the recovery of stranded costs occasioned by open *access*.

1. OPEN ACCESS SHOULD BE APPROACHED ON A CASE-BY-CASE BASIS.

The NCUC and the Public Staff are concerned that the FERC is proposing a generic remedy for a less-than-generic problem. The FERC position that the anti-discrimination provisions of the Federal Power Act (FPA) require across-the-board tariffs for open access to the electric transmission system of every utility is misguided. We recognize that the FERC and various states may disagree about whether a generic approach to open access is legal.[1] Nevertheless, even assuming that such an approach is legal, we believe that a case-by-case approach to open access would be far preferable from a policy standpoint for a number of reasons.

Discriminatory wholesale wheeling rates and discriminatory denial of wholesale access to the electric, utilities' transmission systems vary greatly among the states and are simply not consistently present to the extent necessary to justify a generic approach to open access. The NCUC is unaware of complaints to the FERC by any wholesale customer regarding discriminatory denial of access to **[3]** or of discriminatory rates for use of the transmission system in North Carolina. The absence of such complaints strongly

[1]This legal argument, as we understand it, is based on the fact that § 211 of the FPA, 16 U.S.C. § 824j, as amended by § 721 of the Energy Policy Act of 1992 (the source of the FERC's authority to order wholesale wheeling) provides that the FERC can order a transmitting utility to provide transmission service upon application and after notice and an opportunity for an evidentiary hearing. We will be monitoring with great interest the comments of others with respect to this issue.

suggests that discrimination is not a problem in North Carolina.

If anything, the generic open access proposal by the FERC has the potential to cause undue discrimination where none existed before. For example, the electric transmission system of each utility is interconnected with neighboring transmission systems in order to ensure greater reliability. However, this interconnection exposes each transmission system to greater loop flows.[2] Open access will greatly complicate loop flows by increasing the number of participants contributing to such loop flows, and it will also cause an unfairly disproportionate burden of dealing with the impact of loop flows to fall on many utilities that are not direct participants in an open access wheeling transaction.

[2]As the FERC is well aware, the actual path taken by electric power flow across a transmission system is difficult to predict. Because of its interconnection with neighboring systems, a transmission system typically consists of a number of possible paths between any two points.. Electric current essentially flows on a path of least resistance. An electric load placed on the transmission system will usually cause electric current to flow in all possible paths, but the amount of flow in each path will vary depending on the amount of resistance to flow in a given path. The resulting circuitous route (or mutes) that electric current actually takes in order for electric power to be transferred between two points is called loop flow. In sum, the actual flow of electricity typically diverges significantly from the contract path, with the result that the supposed economics of the contract path frequently have little to do with the actual cost of the power transfer.

Section 211 of the Federal Power Act, as mended by the Energy Policy Act of 1992 (EPACT), provides that an electric utility, power marketing agency or non-utility generator may apply to the FERC for an order requiring access to the electric transmission system ora transmitting utility (including enlargement of transmitting capacity as necessary). Thus, the EPACT clearly contemplates the ordering of wholesale wheeling **upon request**. We believe this reflects a congressional intent for wholesale wheeling to be required on a case-by-case basis and that the FERC should review issues of "undue discrimination" on a case-by-case basis as intended by the EPACT.

The FERC's current generic approach to pricing may well inhibit greater competition in the wholesale generation market. The FERC's authority to require new transmission facilities to be built, for example, is dependent upon the states granting authority for the new facilities to be constructed. Because the granting of a certificate by a state commission for the construction of transmission facilities could well preclude that commission from disallowing recovery in retail rates, many states may be reluctant to grant such authority with little or no assurance that retail ratepayers will not be required by default to carry a disproportionate share of the costs. Of substantial concern in this regard is the fact that many utilities appear to be unwilling to challenge the FERC's authority and/or its determinations with regard to open access because such action is perceived as endangering approval of market based rates for affiliated generating companies. Obviously, to the extent transmission costs are not recovered by the users of the transmission system, there is a danger that the utilities' captive retail ratepayers will end up covering these costs.

* * * * *

[pp. 6-7]

[6]

3. <u>EACH UTILITY'S GENERATING CAPACITY EXPANSION PLAN REFLECTS AN OBLIGATION TO SERVE THAT TRANSCENDS ITS CONTRACTUAL OBLIGATIONS TO CUSTOMERS.</u>

The NCUC and the Public Staffare concerned about the negative impact that open access to the electric transmission system will have on each utility unless its obligation to serve its wholesale customers is waived. State regulators have charged each utility with an obligation to serve at the retail level in their respective states, and the FERC has created a "de facto" obligation to serve at the wholesale level.

The obligation to serve is reflected in each utility's generating capacity expansion plan, and it transcends any contractual obligation the utility may incur with a customer at either the retail level or the wholesale level. Any "reasonable expectation" that a wholesale customer will remain on a utility's system for the duration of the cost to serve that customer is based on the utility's "de facto" obligation to serve and the resulting generating capacity expansion plan. Until the obligation to serve wholesale customers is clarified, the NCUC and other state commissions will have little choice but to require each utility's integrated resource planning to include the assumption that the obligation to serve extends past the expiration date of its wholesale contracts.

Mandatory wholesale wheeling and a utility's obligation to serve wholesale customers are inconsistent with each other. The obligation to serve arises from a utility's monopoly status. If open access to the electric transmission system is required for wholesale customers in order to promote greater competition, then a utility's obligation to serve them must be waived. Otherwise, the utilities are under a handicap and true competition cannot exist. We urge the FERC to recognize this inconsistency.

4. THE DIVISION OF JURISDICTION BETWEEN THE FERC AND THE STATES IN THE OPEN ACCESS PROPOSED RULEMAKING IS NOT SUPPORTED BY THE FPA OR BY CASE LAW.

The NCUC and the Public Staff are concerned that the division of jurisdiction between the FERC itself and the states in the open access proposed rulemaking is not supported by the FPA or the relevant case law. The FERC open access proposal contains the assertion that the FERC has jurisdiction over all transmission facilities, on the assumption that all transmission facilities are interconnected with neighboring transmission systems and are, therefore, directly or indirectly used [7] to serve wholesale customers. While it is generally recognized that the FERC has jurisdiction over transmission facilities serving wholesale customers and over transmission facilities used for inter-utility transactions, the FISA and the case law provide that the FERC has no jurisdiction over facilities used in local distribution. Local distribution facilities have been defined as facilities used to deliver electric energy to the ultimate consumer. Therefore, because retail customers in many instances are served directly off the transmission

system, transmission facilities can be facilities used in local distribution.

Open access to the transmission facilities that directly serve retail customers will invite sham transactions and sham municipalization by those transmission level retail customers seeking to become wholesale customers and thereby gain access to wholesale wheeling. This is an issue that is certain to invite litigation and potentially delay true wholesale open access. An example of this is the case involving Falls Church, Virginia, and Virginia Electric & Power Company. The NCUC and the Public Staff believe that the FERC has underestimated the creativity with which those individuals who are consultants to large retail customers will approach this issue. A significant cottage industry may well arise solely to convert retail customers into wholesale customers, thereby subverting the intent of Congress as expressly set forth in EPACT.

FEDERAL ENERGY REGULATORY COMMISSION
ORDER 888

[Issued April 24, 1996]

Docket Nos. RM95-8-000 and RM94-7-001

Order No. 888

* * * * *

[pp. 31,632 - 31,684]

[31,036]
61 F.R. 21540 (May 10, 1996)

18 CFR Parts 35 and 385

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities

AGENCY: Federal Energy Regulatory Commission, DOE.

ACTION: Final Rule.

SUMMARY: The Federal Energy Regulatory Commission (Commission) is issuing a Final Rule requiring all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce to have on file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service. The Final Rule also permits public utilities and transmitting utilities to seek recovery of legitimate, prudent

and verifiable stranded costs associated with providing open access and Federal Power Act section 211 transmission services. The Commission's goal is to remove impediments to competition in the wholesale bulk power marketplace and to bring **[31,633]** more efficient, lower cost power to the Nation's electricity consumers.

EFFECTIVE DATE: This Final Rule will become effective on July 9, 1996.

FOR FURTHER INFORMATION CONTACT: David D. Withnell (Legal Information -- Docket No. RM95-8-000) Office of the General Counsel Federal Energy Regulatory Commission 888, First Street, NE., Washington, DC 20426 (202) 208-2063

Deborah B. Leahy (Legal Information -- Docket No. RM94-7-001) Office of the General Counsel Federal Energy Regulatory Commission, 888 First Street, NE., Washington, DC 20426 (202) 208-2039

Michael A. Coleman (Technical Information) Office of Electric Power Regulation Federal Energy Regulatory Commission 888, First Street, NE., Washington, DC 20426 (202) 208-1236

SUPPLEMENTARY INFORMATION: In addition to publishing the full text of this document in the Federal Register, the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in the Public Reference Room at 888, First Street, NE., Washington, DC 20426.

The Commission Issuance Posting System (CIPS), an electronic bulletin board service, provides access to the texts of formal documents issued by the Commission. CIPS is available at no charge to the user and may be accessed using a personal computer with a modem by dialing 202-208-1397 if dialing locally, or 1- 800-856-3920 if dialing long distance. CIPS is also available through the Fed World system (by modem or Internet). To access CIPS, set your communications software to 19200, 14400, 12000, 9600, 7200, 4800, 2400, or 1200 bps, full duplex, no parity, 8 data bits and 1 stop bit. The full text of this order will be available on CIPS indefinitely in ASCII and WordPerfect 5.1 format. The complete text on diskette in Wordperfect format may also be purchased from the Commission's copy contractor, La Dorn Systems Corporation, also located in the Public Reference Room at 888 First Street, N.E., Washington, D.C. 20426.

Table of Contents

I. Introduction/Summary
II. Public Reporting Burden
III. Background
IV. Discussion
A. Scope of the Rule
1. Introduction
2. Functional Unbundling
3. Market-based Rates
4. Merger Policy
5. Contract Reform
6. Flow-based Contracting and Pricing
B. Legal Authority
1. Bases for Legal Authority

2. Response to Commenters Opposing our Legal Authority
C. Comparability
1. Eligibility to Receive Non-discriminatory Open Access Transmission
2. Service that Must be Provided by Transmission Provider
3. Who Must Provide Non-discriminatory Open Access Transmission
4. Reservation of Transmission Capacity by Transmission Customers
5. Reservation of Transmission Capacity for Future Use by Utility
6. Capacity Reassignment
7. Information Provided to Transmission Customers
8. Consequences of Functional Unbundling
D. Ancillary Services
1. Definitions and Descriptions
2. Obligations of Transmission Providers and Transmission Customers with Respect to Ancillary Services
3. Unbundling and Bundling Ancillary Services
4. Reassignment of Ancillary Services
5. Pricing of Ancillary Services
6. Accounting for Ancillary Services
E. Real-Time Information Networks
F. Coordination Arrangements: Power Pools, Public Utility Holding Companies, Bilateral Coordination Arrangements, and Independent System Operators
1. Tight Power Pools
2. Loose Pools
3. Public Utility Holding Companies

[31,634]

4. Bilateral Coordination Arrangements
G. Pro Forma Tariff
1. Tariff Provisions That Affect The Pricing Mechanism
2. Priority for Obtaining Service
3. Curtailment Provisions
4. Specific Tariff Provisions
H. Implementation
I. Federal and State Jurisdiction: Transmission/Local Distribution
J. Stranded Costs
1. Justification for Allowing Recovery of Stranded Costs
2. Cajun Electric Power Cooperative, Inc. v. FERC
3. Responsibility for Wholesale Stranded Costs (Whether to Adopt Direct Assignment to Departing Customers)
4. Recovery of Stranded Costs Associated with New Wholesale Requirements Contracts
5. Recovery of Stranded Costs Associated with Existing Wholesale Requirements Contracts
6. Recovery of Stranded Costs Caused by Retail-Turned-Wholesale Customers
7. Recovery of Stranded Costs Caused by Retail Wheeling
8. Evidentiary Demonstration Necessary -- Reasonable Expectation Standard
9. Calculation of Recoverable Stranded Costs
10. Stranded Costs in the Context of Voluntary Restructuring
11. Accounting Treatment for Stranded Costs
12. Definitions, Application, and Summary
K. Other

1. Information Reporting Requirements for Public Utilities
2. Small Utilities
3. Regional Transmission Groups
4. Pacific Northwest
5. Power Marketing Agencies
6. Tennessee Valley Authority
7. Hydroelectric Power
8. Residential Customers
V. Environmental Statement
VI. Regulatory Flexibility Act Certification
VII. Information Collection Statement
VIII. Effective Date
Regulatory Text
Appendices (These Appendices will not appear in the Code of Federal Regulations)
A. List of Section 211 Applications
B. List of Commenters in Docket Nos. RM95-8-000 and RM94-7-001
C. Allegations of Public Utilities Exercising Transmission Dominance
D. Pro Forma Open Access Transmission Tariff
E. List of Group 1 Public Utilities
F. List of Group 2 Public Utilities
G. Legal Analysis of Commission Jurisdiction Over the Rates, Terms and Conditions of Unbundled Retail Transmission In Interstate Commerce
H. U.S. NO/X/ Emissions
Statement of Commissioner Hoecker
Statement of Commissioner Massey

I. Introduction/Summary

Today the Commission issues three final, interrelated rules designed to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers.[1] The legal and policy cornerstone of these rules is to remedy undue discrimination in access to the monopoly owned transmission wires that control whether and to whom electricity can be transported in interstate commerce. A second critical aspect of the **[31,635]** rules is to address recovery of the transition costs of moving from a monopoly-regulated regime to one in which all sellers can compete on a fair basis and in which electricity is more competitively priced.

[1]These rules are the rules on open access and stranded costs in the above dockets (*FERC Statutes and Regulations* ¶31,036), and an accompanying rule on Open Access Same-Time Information System and Standards of Conduct (OASIS Final Rule) (*FERC Statutes and Regulations* ¶31,037) being issued contemporaneously. The Commission also is issuing contemporaneously a notice of proposed rulemaking on capacity reservation open access transmission tariffs in Docket No. RM96-11-000, *FERC Statutes and Regulations* ¶32,517. These final rules and proposed rule are being published concurrently in the *Federal Register*.

In the year since the proposed rules were issued,[2] the pace of competitive changes in the electric utility industry has accelerated. By March of last year, 38 public utilities had filed wholesale open access transmission tariffs with the Commission. Today, prodded by such competitive changes and encouraged by our proposed rules, 106 of the approximately 166 public utilities that own, control, or operate[3] transmission facilities used in interstate commerce have filed some form of wholesale open access tariff. In addition, since the time the proposed rules were issued, numerous state regulatory commissions have adopted or are

[2]On March 29, 1995, the Commission issued two notices of proposed rulemaking concerning open access transmission and stranded cost recovery. Promoting Wholesale Competition Through Open-Access Non-Discriminatory Transmission Service by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, 60 FR 17662 (April 7, 1995), *FERC Statutes and Regulations* ¶32,514 (1995). On December 13, 1995, the Commission issued a notice of proposed rulemaking on information systems. Real- Time Information Networks and Standards of Conduct, Notice of Proposed Rulemaking, 60 FR 66182 (December 21, 1995), *FERC Statutes and Regulations* ¶32,516 (1995).

[3]The Commission's notice of proposed rulemaking in the above dockets proposed to apply the proposed requirements to public utilities that own and/or control facilities used for the transmission of electric energy in interstate commerce. "Own and/or control" is intended to include public utilities that "operate" facilities used for the transmission of electric energy in interstate commerce. However, we have modified the Final Rule regulatory text to remove any ambiguity.

actively evaluating retail customer choice programs or other utility restructuring alternatives. These events have been spurred by continuing pressures in the marketplace for changes in the way electricity is bought, sold, and transported. Increasingly, customers are demanding the benefits of competition in the growing electricity commodity market.

The Commission estimates the potential quantitative benefits from the Final Rule will be approximately $3.8 to $5.4 billion per year of cost savings, in addition to the non-quantifiable benefits that include better use of existing assets and institutions, new market mechanisms, technical innovation, and less rate distortion. The continuing competitive changes in the industry and the prospect of these benefits to customers make it imperative that this Commission take the necessary steps within its jurisdiction to ensure that all wholesale buyers and sellers of electric energy can obtain non-discriminatory transmission access, that the transition to competition is orderly and fair, and that the integrity and reliability of our electricity infrastructure is maintained.

In this Rule, the Commission seeks to remedy both existing and future undue discrimination in the industry and realize the significant customer benefits that will come with open access. Indeed, it is our statutory obligation under sections 205 and 206 of the Federal Power Act (FPA) to remedy undue discrimination.

To do so, we must eliminate the remaining patchwork of closed and open jurisdictional transmission systems and ensure that all these systems, including those that already provide some form of open access, cannot use monopoly

power over transmission to unduly discriminate against others. If we do not take this step now, the result will be benefits to some customers at the expense of others. We have learned from our experience in the natural gas area the importance of addressing competitive transition issues early and with as much certainty to market participants as possible.

Accordingly, in this proceeding and in the accompanying proceeding on OASIS, the Commission, pursuant to its authorities under sections 205 and 206 of the FPA:

•Requires all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce

•To file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service;

[31,636]

•To take transmission service (including ancillary services) for their own new wholesale sales and purchases of electric energy under the open access tariffs;

•To develop and maintain a same-time information system that will give existing and potential transmission users the same access to transmission information that the public utility enjoys, and further requires public utilities to separate transmission from generation marketing functions and communications;

•Clarifies Federal/state jurisdiction over transmission in interstate commerce and local distribution and provides for deference to certain state recommendations; and

•Permits public utilities and transmitting utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and FPA section 211 transmission services.

Open Access

The Final Rule requires public utilities to file a single open access tariff that offers both network, load-based service and point-to-point, contract-based service. The Rule contains a pro forma tariff that reflects modifications to the NOPR's proposed terms and conditions and also permits variations for regional practices. All public utilities subject to the Rule, including those that already have tariffs on file, will be required to make section 206 compliance filings to meet the new pro forma tariff non-price minimum terms and conditions of non-discriminatory transmission. Utilities may propose their own rates in a section 205 compliance filing.

The Rule provides that public utilities may seek a waiver of some or all of the requirements of the Final Rule. In addition, non-public utilities may seek a waiver of the tariff reciprocity provisions.

The Final Rule does not generically abrogate existing requirements contracts, but will permit customers and public utilities to seek modification, or termination, of certain existing requirements contracts on a case-by-case basis. As to coordination arrangements and contracts, the Rule finds that

these arrangements and contracts may need to be modified to remove unduly discriminatory transmission access and/or pricing provisions. Such arrangements and agreements include power pool agreements, public utility holding company agreements, and certain bilateral coordination agreements. The Rule provides guidance and timelines for modifying unduly discriminatory coordination arrangements and contracts, and specifies when the members of such arrangements must begin to conduct trade with each other using the same open access tariff offered to others. The Rule also provides guidance regarding the formation of independent system operators (ISOs).

The Rule does not require any form of corporate restructuring, but will accommodate voluntary restructuring that is consistent with the Rule's open access and comparability policies.

As discussed in the NOPR, not all owners or controllers of interstate transmission facilities are subject to the Commission s jurisdiction under sections 205 and 206 of the FPA and therefore are not subject to this Rule's open access requirements. Therefore, the Final Rule retains the proposed reciprocity provision in the pro forma tariff. Without such a provision, non-open access utilities could take advantage of the competitive opportunities of open access, while at the same time offering inferior access, or no access at all, over their own facilities. Thus, open access utilities would be unfairly burdened. We note that some non-jurisdictional utilities have expressed an interest in a mechanism for obtaining a Commission determination that their transmission tariffs satisfy the reciprocity provisions in

the pro forma tariffs, and we provide such a mechanism in the Rule.

The Final Rule does not generically provide for market-based generation rates. Although the Rule codifies the Commission's prior decision that there is no generation dominance in new generating capacity, intervenors in cases may raise generation dominance issues related to new capacity. In addition, to obtain market-based rates for existing generation, we will continue to require public utilities to show, on a case-by-case basis, that there is no generation dominance in existing capacity. Further, in all market-based rate cases, we will continue to look at whether an applicant and its affiliates could erect other barriers to entry and **[31,637]** whether there may be problems due to affiliate abuse or reciprocal dealing.

Finally, contemporaneously with this Rule the Commission issues a NOPR on capacity reservation tariffs as an alternative, and perhaps superior, means of remedying undue discrimination.

Transmission/Local Distribution

The Rule clarifies the Commission's interpretation of the Federal/state jurisdictional boundaries over transmission and local distribution. While we reaffirm our conclusion that this Commission has exclusive jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, we nevertheless recognize the very legitimate concerns of state regulatory authorities as they contemplate direct retail access or other state restructuring programs. Accordingly, we specify

circumstances under which we will give deference to state recommendations. Although jurisdictional boundaries may shift as a result of restructuring programs in wholesale and retail markets, we do not believe this will change fundamental state regulatory authorities, including authority to regulate the vast majority of generation asset costs, the siting of generation and transmission facilities, and decisions regarding retail service territories. We intend to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies.

Stranded Costs

With regard to stranded costs, the Final Rule adopts the Commission's supplemental proposal. It will permit utilities to seek extra-contractual recovery of stranded costs associated with a limited set of existing (executed on or before July 11, 1994) wholesale requirements contracts and provides that the Commission will be the primary forum for utilities to seek recovery of stranded costs associated with retail-turned-wholesale transmission customers. It also will allow utilities to seek recovery of stranded costs caused by retail wheeling only in circumstances in which the state regulatory authority does not have authority to address retail stranded costs at the time the retail wheeling is required. The Rule retains the revenues lost approach for calculating stranded costs and provides a formula for calculating such costs.

Environmental Issues

The Commission has prepared a Final Environmental Impact Statement (FEIS) evaluating the possible

environmental consequences of changes in the bulk power marketplace expected to occur as a result of the open access requirements of this Final Rule. The FEIS focuses, as do most commenters, on possible increases in emissions of nitrogen oxides (NO/X/) from certain fossil-fuel fired generators, which could affect air quality in the producing region and in areas to which these emissions may be carried.

In response to comments on the Draft EIS, the Commission performed numerous additional studies. The FEIS finds that the relative future competitiveness of coal and natural gas generation is the key variable affecting the impact of the Final Rule. If competitive conditions favor natural gas, the Rule is likely to lead to environmental benefits. Both EPA and the Commission staff believe this projected scenario is the more likely one. If competitive conditions favor coal, the Rule may lead to small negative environmental impacts. However, even using the most extreme, unlikely assumptions about the future of the industry, the negative consequences are not likely to occur until after the turn of the century. Because the impacts will remain modest at least until 2010, there is no need for an interim mitigation program. In addition, even if the data showed more significant negative consequences requiring mitigation, the Commission does not have the statutory authority under the Federal Power Act or the expertise to address this possible far- term problem. The Commission believes, however, that there is time for federal and state air quality authorities to address any potential adverse impact as part of a comprehensive NO_x regulatory program under the Clean Air Act.[4]

---

[4]42 U.S.C. §7401, et seq.

Despite our conclusions regarding the lack of environmental impacts expected to result from the Rule, the Commission has examined a wide variety of proposals for mitigating possible adverse effects. We share the view of most commenters **[31,638]** that the preferred approach for mitigating increased NO/X/ emissions generally is a NO/X/ cap and trading regulatory program comparable to that developed by Congress to address sulfur dioxide emissions in the Clean Air Act Amendments of 1990.[5] The Commission has examined various means of establishing such a program, including use of existing federal authorities under the Clean Air Act, cooperative efforts by state and federal air quality regulators, and development of a new emissions regulatory program administered by the Commission under the Federal Power Act. The Commission has concluded that a NO/X/ regulatory program could best be developed and administered under the Clean Air Act, in cooperation with interested states, and offers to lend Commission support to that effort should it become necessary.

Conclusion

The Commission believes that the Final Rule will remedy undue discrimination in transmission services in interstate commerce and provide an orderly and fair transition to competitive bulk power markets.

---

[5]42 U.S.C.A. §7651b-e.

II. Public Reporting Burden

The Open Access Final Rule and the Stranded Cost Final Rule specify filing requirements to be followed by public utilities that own, control or operate transmission facilities in interstate commerce in making non-discriminatory open access tariff filings and filings to recover legitimate, prudent and verifiable stranded costs. The information collection requirements of the final rules are attributable to FERC-516 "Electric Rate Filings." The current total annual reporting burden for FERC-516 is 828,300 hours.

A. *Docket No. RM95-8-000 (Open Access Final Rule)*

The Open Access Final Rule requires public utilities filing non-discriminatory open access tariffs to provide certain information to the Commission. The Commission estimated that the public reporting burden for the information collection would average 300 hours per response. This estimate included time for reviewing the requirements of the Commission's regulations, searching existing data sources, gathering and maintaining the necessary data, completing and reviewing the collection of information, and filing the revised information. No comments on the burden estimate were received. Because the Final Rule adopts essentially the same information requirements that are contained in the proposed rule, we believe that the average filing burden is same for the Final Rule.

In the proposed rule, the Commission noted that there are approximately 328 public utilities, including marketers and wholesale generation entities. We initially estimated that 137 public utilities own, control or operate facilities used for

the transmission of electric energy in interstate commerce, and would be subject to the filing requirements of the proposed rule. Upon further review, the Commission believes that approximately 166 public utilities will respond to the information collection. Accordingly, the public reporting burden is estimated to be 49,800 hours.

B. *Docket No. RM94-7-001 (Stranded Cost Final Rule)*

In the supplemental notice of proposed rulemaking, the Commission estimated that the information requirements of the proposed rule would not differ substantially from those contained in the initial proposed rule. In that notice, the Commission estimated that the public reporting burden for the information requirements contained in the proposed rule would be 50 hours per response with 10 responses annually. No comments on this filing burden were received. The information requirements adopted in the Stranded Cost Final Rule are not substantially different from those in the proposed rule. Therefore, the Commission concludes that there will be no additional public filing burden associated with the Stranded Cost Final Rule.

III. Background

In the NOPR, we set out a detailed statement of the events leading up to this rulemaking. We repeat that background here, updated to reflect what has happened since March 1995, and discuss why it is necessary to undertake regulatory reform in the electric industry at this time. We do so to provide the necessary **[31,639]** backdrop to our action in adopting this Rule.

A. *Structure of the Electric Industry at Enactment of Federal Power Act*

The Federal Power Act was enacted in an age of mostly self-sufficient, vertically integrated electric utilities, in which generation, transmission, and distribution facilities were owned by a single entity and sold as part of a bundled service (delivered electric energy) to wholesale and retail customers. Most electric utilities built their own power plants and transmission systems, entered into interconnection and coordination arrangements with neighboring utilities, and entered into long-term contracts to make wholesale requirements sales (bundled sales of generation and transmission) to municipal, cooperative, and other investor-owned utilities (IOUs) connected to each utility's transmission system. Each system covered limited service areas. This structure of separate systems arose naturally due primarily to the cost and technological limitations on the distance over which electricity could be transmitted.

Through much of the 1960s, utilities were able to avoid price increases, but still achieve increased profits, because of substantial increases in scale economies, technological improvements, and only moderate increases in input prices.[6] Thus, there was no pressure on regulatory

[6]Paul L. Joskow, Inflation and Environmental Concern: Structural Change in the Process of Public Utility Regulation, 17 J. Law & Econ. 291, 312 (1974); *see also* Charles F. Phillips, Jr., *The Regulation of Public Utilities* 11 (1988).

commissions to use regulation to affect the structure of the industry.[7]

B. *Significant Changes in the Electric Industry*

In the late 1960s and throughout the 1970s, a number of significant events occurred in the electric industry that changed the perceptions of utilities and began a shift to a more competitive marketplace for wholesale power.[8] This was the beginning of periods of rapid inflation, higher nominal interest rates, and higher electricity rates.[9] During this time, consumers became concerned about higher electricity rates and questioned any price increases filed by utilities.[10]

During this same time frame, the construction of nuclear and other capital-intensive baseload facilities--actively encouraged by federal and some state governments--contributed to the continuing cost increases and uncertainties

[7]*See* Joskow, *supra* at p. 312; *see also* Phillips, *supra* at p. 12.

[8]*See* Joskow, *supra* at p. 312; *see also* Phillips, *supra* at pp. 12-13.

[9]*See* Joskow, *supra* at pp. 312-13; *see also* Phillips, supra at p. 13. The Arab oil embargo resulted in significantly higher oil prices through the 1970s. *See* Richard J. Pierce, Jr., The Regulatory Treatment of Mistakes in Retrospect: Canceled Plants and Excess Capacity, 132 U. Pa. L. Rev. 497, 501 (1984).

[10]*See* Joskow, *supra* at p. 313; *see also* Phillips, *supra* at p. 13.

in the industry.[11] These investments were made based on the assumptions that there would be steady increases in the demand for electricity and continued large increases in the price of oil.[12] However, due to conservation and economic downturns, the expected demand increases did not materialize. Load growth virtually disappeared in some areas, and many utilities unexpectedly found themselves with excess capacity.[13] In addition, by the 1980s, the oil cartel collapsed, with a resulting glut of low-priced oil.[14] At the same time, inflation substantially increased the costs of these large baseload generating plants.[15] Surging interest rates further increased the cost of the capital needed to finance and capitalize these projects and completion schedules were

---

[11]*See generally Jersey Central Power & Light Company v. FERC*, 810 F.2d 1168, 1171 (D.C. Cir. 1987).

[12]*Id.*

[13]*See* Pierce, *supra* at 503. By 1983, the Department of Energy had estimated that the sunk costs for canceled nuclear plants alone amounted to $10 billion. *Id.* at 498.

[14]*Id.*

[15]*See* Bernard S. Black & Richard J. Pierce, Jr., The Choice Between Markets and Central Planning in Regulating the U.S. Electricity Industry, 93 Col. L. Rev. 1339, 1346 (1993) ("Actual costs of nuclear power plants vastly exceeded estimates, sometimes by as much as 1000%.").

significantly **[31,640]** extended by, in part, more stringent safety and environmental requirements.[16]

As a result, expensive large baseload plants for which there was little or no demand, came onto the market or were in the process of being constructed. Accordingly, between 1970 and 1985, average residential electricity prices more than tripled in nominal terms, and increased by 25% after adjusting for general inflation.[17] Moreover, average electricity prices for industrial customers more than quadrupled in nominal terms over the same period and increased 86% after adjusting for inflation.[18] The rapidly increasing rates for electric power during this period, together with the opportunities provided by the Public Utility Regulatory

---

[16]*See* Phillips, *supra* at p. 13. Fossil fuel-fired plants became subject to increased regulation as a result of the Clean Air Act of 1970, and its 1977 amendments. 42 U.S.C. §§7401-7642. In 1971, nuclear plant licensing became subject to the environmental impact statement requirements of the National Environmental Policy Act of 1969. 42 U.S.C. §4332. Following the 1979 accident at the Three Mile Island nuclear plant, nuclear plants also became subject to additional safety regulations, resulting in higher costs. *See* Energy Information Administration, *The Changing Structure of the Electric Power Industry 1970-1991* (March 1993) 35. Between 1976 and 1980, most states and many localities instituted laws governing power plant siting.

[17]Based on retail prices reported in Energy Information Administration (EIA), Monthly Energy Review, January 1995, Table 9.9 (Prices adjusted for inflation using the GDP Deflator (1987 = 100)).

[18]*Id.*

Policies Act of 1978 (PURPA) (discussed infra), also prompted some industrial customers to bypass utilities by constructing their own generation facilities. This further exacerbated rate increases for remaining customers -- primarily residential and commercial customers.

Consumers responded to these "rate shocks" by exerting pressure on regulatory bodies to investigate the prudence of management decisions to build generating plants, especially when construction resulted in cost overruns, excess capacity, or both. Between 1985 and 1992, writeoffs of nuclear power plants totalled $22.4 billion.[19] These writeoffs significantly reduced the earnings of the affected utilities.[20] Delays in obtaining rate increases to reflect the effects of inflation further reduced investor returns. Thus, many utilities became reluctant to commit capital to long-term construction decisions involving large scale generating plants.[21]

In addition to economic changes in the industry, significant technological changes in both generation and transmission have occurred since 1935. Through the 1960s, bigger was cheaper in the generation sector and the industry was able to capitalize on economies of scale to produce power

---

[19]*See* Black & Pierce, *supra* at p. 1346 (These writeoffs were "about 17% of the book value of total 1992 utility investment.").

[20]*Id.*

[21]*Id.* ("The high perceived risk of future disallowances reversed utilities' incentives to overinvest, and made utilities extremely reluctant to build new power plants.").

at lower per-unit costs from larger and larger plants.[22] As a result, large utility companies that could finance and manage construction projects of larger scale had a price advantage over smaller utility companies and customers who might otherwise have considered building their own generating units. Scale economies encouraged power generation by large vertically-integrated utility companies that also transmitted and distributed power. Beginning in the 1970s, however, additional economies of scale in generation were no longer being achieved.[23] A significant factor was that larger generation units were found to need relatively greater maintenance and experience longer downtimes.[24] The electric **[31,641]** industry faced the situation "where the price of each incremental unit of electric power exceeded the average cost."[25] Bigger was no longer better.

---

[22]*See* Preston Michie, Billing Credits for Conservation, Renewable, and Other Electric Power Resources: an Alternative to Marginal-Cost-Based Power Rates in the Pacific Northwest, 13 Environmental Law 963, 964-65 (1983).

[23]*Id.* at p. 965.

[24]Energy Information Administration, *The Changing Structure of the Electric Power Industry 1970-1991* (March 1993) 37 ("As larger units were constructed, however, utilities discovered that downtime was as much as 5 times greater for units larger than 600 megawatts than for units in the 100-megawatt range.")

[25]*Id.*; *see also* George A. Perrault, Downsizing Generation: Utility Plans for the 1990s, Pub. Util. Fort. 15-16 (Sept. 27, 1990) ("The large base-load generating units that form the backbone of utility systems are almost totally absent from capacity plans for the 1990s.").

Further dictating against larger generation units were advances in technologies that allowed scale economies to be exploited by smaller size units, thereby allowing smaller new plants to be brought on line at costs below those of the large plants of the 1970s and earlier. Such new technologies include combined cycle units and conventional steam units that use circulating fluidized bed boilers.[26]

The combined cycle generating plants generally use natural gas as their primary fuel. This technology has been made possible by the development of more efficient gas turbines, shorter construction lead times, lower capital costs, increased reliability, and relatively minimal environmental impacts.[27] Similarly, the circulating fluidized bed combustion boilers, fueled by coal and other conventional fuels, provide a more efficient and less polluting resource.

Today, "the optimum size (of generation plants) has shifted from (more than 500 MW) (10-year lead time) to smaller units (one-year lead time) (in the 50- to 150-MW

---

[26]"From 1982 through 1991, the average capacity of fluidized-bed units increased rapidly to 72 megawatts for 4 units in 1991. The average capacity for the 19 units planned to begin operating in 1992 through 1995 increases to 83 megawatts." Energy Information Administration, *The Changing Structure of the Electric Power Industry 1970-1991* (March 1993) 38.

[27]*See* Charles E. Bayless, Less is More: Why Gas Turbines Will Transform Electric Utilities, Pub. Util. Fort. (Dec. 1, 1994) 21.

range)."[28] Indeed, smaller and more efficient gas-fired combined-cycle generation facilities can produce power on the grid at a cost ranging from 5 cents per kWh to less than 3 cents per kWh.[29] This is significantly less than the costs for large plants constructed and installed by utilities over the last decade, which were typically in the range of 4 to 7 cents per kWh for coal plants and 9 to 15 cents for nuclear plants.[30] Significant changes have also occurred in the transmission sector of the industry. Technological advances in transmission have made possible the economic transmission of electric power over long distances at higher voltages.[31] This has made

---

[28]*Id.* at p. 24. *See also* Wallace E. Brand, Is Bigger Better? Market Power in Bulk Power Supply: From FDR to NOPR, Pub. Util. Fort. (Feb. 15, 1996) 23 at p. 25 (while the optimal baseload unit size is about 500 MW for coal-fired steam turbines, the optimal size for gas fired combined-cycle units is about 150 to 200 MW).

[29]FERC staff calculations based in part on combined-cycle plant cost data reported in 1994 FERC Form No. 1 for a sample of units placed in service during 1990-94. Costs vary with regional fuel and construction costs, among other reasons.

[30]Coal and Nuclear plant cost data reported in 1994 FERC Form No. 1 and the EIA report, *Electric Plant Cost and Power Production Expenses 1991*, 1993 DOE/EIA-0455(91), for plants placed in service during 1986-94; *see also* The 1994 Electric Executives' Forum, Bakke (President and CEO of the AES Corporation), Pub. Util. Fort. (June 1, 1994) 45 ("New generation can be built at about 3 cents per kilowatt-hour (U.S. average). Old generation costs about twice that * * *").

[31]*See* Black & Pierce, *supra* at p. 1345 (In the late 1960s and 1970s, improved transmission efficiency and development of

it technically feasible for utilities with lower cost generation sources to reach previously isolated systems where customers had been captive to higher cost generation. In addition, the nature and magnitude of coordination transactions[32] have changed dramatically since enactment of the FPA, allowing increased coordinated operations and reduced reserve margins. Substantial amounts of electricity now move between regions, as well as between utilities in the same region. Physically isolated systems have become a thing of the past.

[31,642]

C. *The Public Utility Regulatory Policies Act and the Growth of Competition*

In enacting PURPA,[33] Congress recognized that the rising costs and decreasing efficiencies of utility-owned generating facilities were increasing rates and harming the

---

regional transmission networks "made it possible to build power plants up to 1000 miles from power users.").

[32]Coordination transactions are voluntary sales or exchanges of specialized electricity services that allow buyers to realize cost savings or reliability gains that are not attainable if they rely solely on their own resources. For sellers, these transactions provide opportunities to earn additional revenue, and to lower customer rates, from capacity that is temporarily excess to native load capacity requirements.

[33]Pub. L. No. 95-617, 92 Stat. 3117 (codified in U.S.C. sections 15, 16, 26, 30, 42, and 43).

economy as a whole.[34] To lessen dependence on expensive foreign oil, avoid repetition of the 1977 natural gas shortage, and control consumer costs, Congress sought to encourage electric utilities to conserve oil and natural gas.[35] In particular, Congress sanctioned the development of alternative generation sources designated as "qualifying facilities" (QFs) as a means of reducing the demand for traditional fossil fuels.[36] PURPA required utilities to purchase power from QFs

---

[34]*See generally FERC v. Mississippi*, 456 U.S. 742, 745-46 (1982).

[35]The Power Plant and Industrial Fuel Use Act of 1978. Pub. L. No. 95-617, 92 Stat. 3117 (codified in U.S.C. sections 15, 16, 26, 30, 42, and 43).

[36]QFs include certain cogenerators and small power producers. PURPA also added sections 210, 211, and 212 to the FPA, providing the Commission with authority to approve applications for interconnections and, in limited circumstances, wheeling. However, under section 211, as enacted in PURPA, the Commission could approve an application for wheeling only if it found, inter alia, that the order "would reasonably preserve existing competitive relationships." Because of this and other limitations in sections 211 and 212 as originally enacted, the provision was virtually ineffective. Only one section 211 order was ever issued pursuant to the original provision, and it was pursuant to a settlement. *See Public Service Company of Oklahoma*, 38 FERC ¶61,050 (1987). As discussed *infra*, section 211 was subsequently revised by the Energy Policy Act of 1992.

at a price not to exceed the utility's avoided costs and to sell backup power to QFs.[37]

PURPA specifically set forth limitations on who, and what, could qualify as QFs. In addition to technological and size criteria, PURPA set limits on who could own QFs.[38] Notwithstanding these limitations, QFs proliferated. In 1989, there were 576 QF facilities. By 1993, there were more than 1,200 such facilities.[39] For the same time period, installed QF capacity increased from 27,429 megawatts to 47,774 megawatts.[40] The rapid expansion and performance of the QF industry demonstrated that traditional, vertically integrated public utilities need not be the only sources of reliable power.

---

[37]456 U.S. at p. 750. Congress recognized that encouragement was needed in part because utilities had been reluctant to purchase electric power from, and sell power to, nonutility generators. *Id.* at pp. 750-51.

[38]For example, PURPA provided that a cogeneration facility or small power production facility could not be owned by a person primarily engaged in the generation or sale of electric power (other than from cogeneration or small power production facilities). *See* 16 U.S.C.

[39]Energy Information Administration, *Electric Power Annual 1993* (December 1994) 124 (Table 77).

[40]*Id.* EIA data for 1989 through 1991 was for facilities of 5 megawatts or more and for 1992 and 1993 was for facilities of 1 megawatt or more. A comparison with Table 74 on page 121 for the years 1992 and 1993 reveals that this mixing of data bases is likely of minimal effect.

During this period, the profile of generation investment began to change, and a market for non-traditional power supply beyond the purchases required by PURPA began to emerge. QFs were limited to cogenerators and small power producers.[41]

However, other non-traditional power producers who could not meet the QF criteria began to build new capacity to compete in bulk power markets, without such PURPA benefits as the mandatory purchase requirements. These producers, known as independent power producers (IPPs), were predominantly single-asset generation companies that did not own any transmission or distribution facilities. While traditional utilities were generally **[31,643]** reluctant at that time to invest in new generating facilities under cost of service regulation, utilities increasingly became interested in participating in this new generation sector. They organized affiliated power producers (APPs), with assets not included in utility rate base, and sought to sell power in their own service territories and the territories of other utilities. At the same

---

[41]Generally, the law has imposed an 80 MW cap on small power producers. A limited exception enacted in 1990 permitted small power facilities that could exceed 80 MW and still qualify as QFs under PURPA. This exception was limited to certain solar, wind, waste, and geothermal small power production facilities and only covered applications for certification of facilities as qualifying small power production facilities that were submitted no later than December 31, 1994 and for which construction commences no later than December 31, 1999. See Solar, Wind, Waste, and Geothermal Power Production Incentives Act of 1990, Pub. L. No. 101-575, 104 Stat. 2834 (1990), *amended*, Pub. L. No. 102-46, 105 Stat. 249 (1991).

time, power marketers arose. These entities -- owning no transmission or generation -- buy and sell power.[42]

There were two major impediments to the development of IPPs and APPs. First, the ownership restrictions of the Public Utility Holding Company Act (PUHCA)[43] severely inhibited these new entities from entering the generation business.[44] Second, these entities needed transmission service in order to compete in electricity markets.

While the Commission had no authority to remove PUHCA restrictions,[45] it encouraged the development of IPPs and APPs, as well as emerging power marketers, by authorizing market-based rates for their power sales on a case-by-case basis and by encouraging more widely available transmission access. From 1989 through 1993, facilities owned by IPPs and other non-traditional generators (other

---

[42]The first power marketer in the electric industry was Citizens Energy Corporation. *See Citizens Energy Corporation*, 35 FERC ¶61,198 (1986). Power marketers take title to electric energy. Power brokers, on the other hand, do not take title and are limited to a matchmaking role.

[43]15 U.S.C. §79 *et seq.*

[44]As discussed *infra*, Congress eventually provided a means to avoid the PUHCA restrictions by creating exempt wholesale generators (EWGs) in the Energy Policy Act.

[45]The industry was successful to some extent in developing ownership structures that permitted such investment. *See, e.g., Commonwealth Atlantic Limited Partnership*, 51 FERC ¶61,368 at p. 62,240 and n.20 (1990).

than QFs) increased from 249 to 634 and their installed capacity increased from 9,216 megawatts to 13,004 megawatts.[46] Indeed, "[i]n 1992, for the first time, generating capacity added by independent producers exceeded capacity added by utilities."[47]

Market-based rates helped to develop competitive bulk power markets. A generating utility allowed to sell its power at market-based rates could move more quickly to take advantage of short-term or even long-term market opportunities than those laboring under traditional cost-of-service tariffs, which entail procedural delays in achieving tariff approvals and changes.

In approving these market-based rates, the Commission required, inter alia, that the seller and any of its affiliates lack market power or mitigate any market power that they may have possessed.[48] The major concern of the Commission was whether the seller or its affiliates could limit competition and thereby drive up prices. A key inquiry

---

[46]Energy Information Administration, *Electric Power Annual 1993* (December 1994) 124 (Table 77).

[47]Black & Pierce, *supra* at p. 1349 n.25.

[48]*See, e.g., Ocean State Power*, 44 FERC ¶61,261 (1988); *Commonwealth Atlantic Limited Partnership*, 51 FERC ¶61,368 (1990); *Citizens Power & Light Company*, 48 FERC ¶61,210 (1989); *Orange and Rockland Utilities, Inc.*, 42 FERC ¶61,012 (1988); *Doswell Limited Partnership*, 50 FERC ¶61,251 (1990) (Doswell); and *Dartmouth Power Associates Limited Partnership*, 53 FERC ¶61,117 (1990).

became whether the seller or its affiliates owned or controlled transmission facilities in the relevant service area and therefore, by denying access or imposing discriminatory terms or conditions on transmission service, could foreclose other generators from competing.[49] As we have previously explained:

> The most likely route to market power in today's electric utility industry lies through ownership or control of transmission facilities. Usually, the source of market power is dominant or exclusive ownership of the facilities. However, market power also may be gained without ownership. Contracts can confer the same rights of control. Entities with contractual control over transmission facilities can withhold supply and extract monopoly prices just as effectively as those who control facilities through ownership.[50]

As entry into wholesale power generation markets increased, the ability of customers to gain access to the transmission services necessary to reach competing **[31,644]**

---

[49]*See, e.g., Doswell,* 50 FERC at p. 61,757.

[50]*Citizens Power & Light Corporation*, 48 FERC ¶61,210 at p. 61,777 (1989) (emphasis in original); *see also Utah Power & Light Company, PacifiCorp and PC/UP&L Merging Corporation*, 45 FERC ¶61,095 at pp. 61,287-89 (1988), *order on reh'g*, 47 FERC ¶61,209, *order on reh'g*, 48 FERC ¶61,035 (1989), *remanded in part sub nom. Environmental Action, Inc. v. FERC*, 939 F.2d 1057 (D.C. Cir. 1991), *order on remand*, 57 FERC ¶61,363 (1991).

suppliers became increasingly important.[51] In addition, beginning in the late 1980s, in order to mitigate their market power to meet Commission conditions, public utilities seeking Commission approval of mergers or consolidations under section 203 of the FPA or Commission authorization for blanket approval of market-based rates for generation services under section 205 of the FPA, filed "open access" transmission tariffs of general applicability.[52] The

---

[51]In earlier years, a few customers were able to obtain access as a result of litigation, beginning with the Supreme Court's decision in *Otter Tail Power Company v. United States*, 410 U.S. 366 (1973). Additionally, some customers gained access by virtue of Nuclear Regulatory Commission license conditions and voluntary preference power transmission arrangements associated with federal power marketing agencies. *See, e.g., Consumers Power Company*, 6 NRC 887, 1036-44 (1977) and *The Toledo Edison Company and Cleveland Electric Illuminating Company*, 10 NRC 265, 327-34 (1979). *See Florida Municipal Power Agency v. Florida Power and Light Company*, 839 F. Supp. 1563 (M.D. Fla. 1993). *See also* Electricity Transmission: Realities, Theory and Policy Alternatives, The Transmission Task Force Report to the Commission, October 1989, 197.

[52]*See, e.g., Public Service Company of Colorado*, 59 FERC ¶61,311 (1992), *reh'g denied*, 62 FERC ¶61,013 (1993); *Utah Power & Light Company, et al.*, Opinion No. 318, 45 FERC ¶61,095 (1988), *order on reh'g*, Opinion No. 318-A, 47 FERC ¶61,209 (1989), *order on reh'g*, Opinion No. 318-B, 48 FERC ¶61,035 (1989), *aff'd in relevant part sub nom. Environmental Action Inc. v. FERC*, 939 F.2d 1057 (D.C. Cir. 1991); *Northeast Utilities Service Company (Public Service Company of New Hampshire)*, Opinion No. 364-A, 58 FERC ¶61,070, *reh'g denied*, Opinion No. 364-B, 59 FERC ¶61,042, *order granting motion to*

Commission applied its market rate analysis to IOUs, as well as IPPs, APPs, and marketers, and allowed IOUs to sell at market-based rates only if they opened their transmission systems to competitors.[53] The Commission also approved proposed mergers on the condition that the merging companies remedy anticompetitive effects potentially caused by the merger by filing "open access" tariffs. These early "open access" tariffs required only that the companies provide point-to-point transmission services, which is a much narrower requirement than that being imposed in this Rule and did not require transmission owners to provide to others the same quality of service that they themselves enjoyed.

Following PURPA, the economic and technological changes in the transmission and generation sectors helped give impetus to the many new entrants in the generating markets who could sell electric energy profitably with smaller scale technology at a lower price than many utilities selling from their existing generation facilities at rates reflecting cost. However, it became increasingly clear that the potential consumer benefits that could be derived from these technological advances could be realized only if more efficient generating plants could obtain access to the regional transmission grids. Because many traditional vertically

---

vacate and dismissing request for rehearing, 59 FERC ¶61,089 (1992), *affirmed in relevant part sub nom. Northeast Utilities Service Company v. FERC*, 993 F.2d 937 (1st Cir. 1993).

[53]*See, e.g., Public Service of Indiana, Inc.*, 51 FERC ¶61,367 (1990), *reh'g denied*, 52 FERC ¶61,260 (1990), *appeal dismissed sub nom. Northern Indiana Public Service Company v. FERC*, 954 F.2d 736 (D.C.Cir. 1992).

integrated utilities still did not provide open access to third parties and still favored their own generation if and when they provided transmission access to third parties, barriers continued to exist to cheaper, more efficient generation sources.

D. *The Energy Policy Act*

In response to the competitive developments following PURPA, and the fact that PUHCA and lack of transmission access remained major barriers to new generators, Congress enacted Title VII of the Energy Policy Act of 1992 (Energy Policy Act).[54] A goal of the Energy Policy Act was to promote greater competition in bulk power markets by encouraging new generation entrants, known as exempt wholesale generators (EWGs), and **[31,645]** by expanding the Commission's authority under sections 211 and 212 of the FPA to approve applications for transmission services.[55]

An EWG is defined as

---

[54]Pub. L. No. 102-486, 106 Stat. 2776 (1992), codified at, among other places, 15 U.S.C. §79z-5a and 16 U.S.C. §796(22-25), 824j-l.

[55]*See El Paso Electric Company and Central and South West Services Inc.*, 68 FERC ¶61,181 at p. 61,914 (1994) (CSW); *see also* Paul Kemezis, FERC's Competitive Muscle: The Comparability Standard, Electrical World 45 (Jan. 1995) ("In EPAct, Congress made it clear that the electric-power industry was to move toward a fully competitive market system, but left most of the implementation to FERC.").

Any person determined by the Federal Energy Regulatory Commission to be engaged directly, or indirectly through one or more affiliates as defined in [PUHCA] section 2(a)(11)(B), and exclusively in the business of owning or operating, or both owning and operating, all or part of one or more eligible facilities and selling electric energy at wholesale.[56]

If the Commission, upon an application, determines that a person is an EWG, that person will be exempt from PUHCA.[57] This provision removed a significant impediment to the development of IPPs and APPs by allowing them to develop projects as EWGs free from the strictures of PUHCA or the QF PURPA limitations.

While sections 211 and 212, as enacted by PURPA, were intended to provide greater access to the transmission grid, the limitations placed on these sections made them unusable in virtually all circumstances.[58] However, as amended by the Energy Policy Act, these sections now give the Commission broader authority to order transmitting utilities to provide wholesale transmission services, upon application, to any electric utility, Federal power marketing agency, or any other person generating electric energy for sale for resale.

---

[56]15 U.S.C. §79z-5a.

[57]15 U.S.C. §79z-5a(e).

[58]*See supra* note 36.

The Energy Policy Act also added section 213 to the FPA. Section 213(a) requires a transmitting utility that does not agree to provide wholesale transmission service in accordance with a good faith request to provide a written explanation of its proposed rates, terms, and conditions and its analysis of any physical or other constraints.[59] Section 213(b) required the Commission to enact a rule requiring transmitting utilities to submit annual information concerning potentially available transmission capacity and known constraints.[60]

E. *The Present Competitive Environment*

Following the Energy Policy Act, the Commission established rules: (1) for certain generators to obtain EWG

---

[59]*See* Policy Statement Regarding Good Faith Requests for Transmission Services and Responses by Transmitting Utilities Under Sections 211(a) and 213(a) of the Federal Power Act, as Amended and Added by the Energy Policy Act of 1992, 58 FR 38964 (July 21, 1993), FERC Statutes and Regulations ¶30,975 (1993) (Policy Statement Regarding Good Faith Requests for Transmission Services).

[60]*See* New Reporting Requirements Implementing Section 213(b) of the Federal Power Act and Supporting Expanded Regulatory Responsibilities Under the Energy Policy Act of 1992, and Conforming and Other Changes to Form No. FERC-714, 58 FR 52420 (October 8, 1993), FERC *Statutes and Regulations* ¶30,980 (Order No. 558), *reh'g denied*, Order No. 558-A, 65 FERC ¶61,324 (1993), *regulations modified*, 59 FR 15333 (April 1, 1994), FERC *Statutes and Regulations* ¶30,993.

status and thus an exemption from PUHCA;[61] and (2) that required transmission information availability. The Commission also pursued a number of initiatives aimed at fostering the development of more competitive bulk power markets, including aggressive implementation of section 211, a new look at undue discrimination under the FPA, easing of market entry for sellers of generation from new facilities, and initiation of a number of industry-wide reforms. As stated by the Commission, in recognition of the Congressional goal in **[31,646]** the Energy Policy Act of creating competitive bulk power markets:

Our goal is to facilitate the development of competitively priced generation supply options, and to ensure that wholesale purchasers of electric energy can reach alternative power suppliers and vice versa.[62]

---

[61]*See* Order No. 550, Filing Requirements and Ministerial Procedures for Persons Seeking Exempt Wholesale Generator Status, 58 FR 8897 (February 18, 1993), *FERC Statute and Regulations* ¶30,964, *order on reh'g*, Order No. 550-A, 58 FR 21250 (April 20, 1993), *FERC Statutes and Regulations* ¶30,969 (1993). As recognized by Congress and the Commission, availability of transmission information is critical in developing competitive markets. *See supra* notes 59 and 60. This opened the "black box" of information that previously was available only to transmission owners.

[62]*See* Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking, 59 FR 35274 (July 11, 1994), FERC *Statutes and Regulations* ¶32,507 at p. 32,866 (Stranded Cost NOPR); *American Electric Power Service Corporation*, 67 FERC ¶61,168, *clarified*, 67 FERC ¶61,317 (1994).

1. Use of Sections 211 and 212 to Obtain Transmission Access

The Commission has aggressively implemented sections 211 and 212 of the FPA, as amended by the Energy Policy Act, in order to promote competitive markets.[63] When wheeling requests under sections 211 and 212 have been made, the Commission has required wheeling in almost all of the requests it has processed. To date, the Commission has issued orders (proposed or final) requiring wheeling in 12 of the 14 cases it has acted on.[64]

As a general matter, section 211 has permitted some inroads to be made by customers in obtaining transmission service from public utilities that historically have declined to provide access to their systems, or have offered service only on a discriminatory basis. Under section 211, the Commission has granted requests for the broader type of service that most utilities historically have refused to provide -- network service. Although transmission owners have provided limited amounts of unbundled point-to-point transmission service, third- party customers have not been able to obtain the flexibility of service that transmission owners enjoy.

---

[63]16 U.S.C.A. §§824j-824k (West 1985 and Supp. 1994).

[64]*See, e.g.*, final orders issued in *City of Bedford*, 68 FERC ¶61,003 (1994), *reh'g denied*, 73 FERC ¶61,322 (1995); *Florida Municipal Power Agency v. Florida Power & Light Company*, 67 FERC ¶61,167 (1994), *order on reh'g*, 74 FERC ¶61,006 (1996); *Minnesota Municipal Power Agency*, 68 FERC ¶61,060 (1994); and *Tex-La Electric Cooperative of Texas*, 69 FERC ¶61,269 (1994); *see also* Appendix A.

In Florida Municipal, a section 211 case, the Commission ordered "network," rather than the narrower "point-to-point," service.[65] Network service permits the applicant to fully integrate load and resources on an instantaneous basis in a manner similar to the transmission owner's integration of its own load and resources. At the same time, the Commission made the generic finding that the availability of transmission service will enhance competition in the market for power supplies and lead to lower costs for consumers. The Commission explained that as long as the transmitting utility is fully and fairly compensated and there is no unreasonable impairment of reliability, transmission service is in the public interest.[66]

As discussed infra, based on the mounting competitive pressures in the industry and rapidly evolving markets, we

---

[65]*See Florida Municipal Power Agency v. Florida Power & Light Company*, 65 FERC ¶61,125, *reh'g dismissed*, 65 FERC ¶61,372 (1993), *final order*, 67 FERC ¶61,167 (1994), *order on reh'g*, 74 FERC ¶61,006 (1996). The Commission has "characterized point-to-point service as involving designated points of entry into and exit from the transmitting utility's system, with a designated amount of transfer capability at each point." *El Paso Electric Company v. Southwestern Public Service Company*, 68 FERC ¶61,182 at p. 61,926 n.9 (1994) (*citing Entergy Services, Inc.*, 58 FERC ¶61,234 at p. 61,768 (1993), *reh'g dismissed*, 68 FERC ¶61,399 (1994)). Network service allows more flexibility by allowing a transmission customer to use the entire transmission network to provide generation service for specified resources and specified loads without having to pay multiple charges for each resource-load pairing.

[66]*Florida Municipal*, 67 FERC at p. 61,477.

have concluded that section 211 alone is not enough to eliminate undue discrimination. The comments received on the proposed rules, discussed in detail infra, confirm this conclusion. The significant time delays involved in filing an individual service request for bilateral service under section 211 place the customer at a severe disadvantage compared to the transmission owner and can result in discriminatory treatment in the use of the transmission system. It is an inadequate procedural substitute for readily available service under a filed non-discriminatory open access tariff. As the Commission noted in Hermiston Generating Company, **[31,647]** "[t]he ability to spend time and resources litigating the rates, terms and conditions of transmission access is not equivalent to an enforceable voluntary offer to provide comparable service under known rates, terms and conditions."[67]

2. Commission's Comparability Standard

In the Spring of 1994, the Commission began to address the problem of the disparity in transmission service that utilities provided to third parties in comparison to their own uses of the transmission system. In the seminal case in this area, American Electric Power Service Corporation (AEP), the company voluntarily proposed a tariff of general applicability that would offer firm, point-to-point transmission

---

[67]69 FERC ¶61,035 at p. 61,165 (1994), *reh'g denied*, 72 FERC ¶61,071 (1995); *see also Southwest Regional Transmission Association*, 69 FERC ¶61,100 at p. 61,398 (1994), *order on compliance filing*, 73 FERC ¶61,147 (1995) *(SWRTA)*.

service for a minimum of one month.[68] The Commission accepted the proposed transmission tariff for filing and suspended its effectiveness for one day, subject to refund.[69] Rehearing requests challenged the Commission's summary approval of the restriction of service to point-to-point as being discriminatory and anticompetitive.[70] The rehearing requests argued that the tariff should be expanded to include network services such as those used by the transmission owner. On rehearing, the Commission announced a new standard for evaluating claims of undue discrimination.

The Commission found that a voluntarily offered, new open access transmission tariff that did not provide for services comparable to those that the transmission owner provided itself was unduly discriminatory and anticompetitive.[71] In reaching that conclusion, the

---

[68]64 FERC 61,279 (1993), *reh'g granted*, 67 FERC ¶61,168, *clarified*, 67 FERC ¶61,317 (1994).

[69]The Commission explained that AEP could limit the service it was offering because it was "providing the service voluntarily under a tariff of general applicability." 64 FERC at p. 62,978.

[70]*AEP*, 67 FERC at p. 61,489.

[71]With respect to anticompetitive effects, the Commission explained that it has "adhered to the Supreme Court's determination that the Commission's 'important and broad regulatory power * * * carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of interstate utility operations pursuant to sections 202 and 203, and under like directives contained in sections 205, 206 and 207.' *Gulf*

Commission broadened its undue discrimination analysis (which traditionally had focused on the rates, terms, and conditions faced by similarly situated third- party customers) to include a focus on the rates, terms, and conditions of a utility's own uses of the transmission system:

> (A)n open access tariff that is not unduly discriminatory or anticompetitive should offer third parties access on the same or comparable basis, and under the same or comparable terms and conditions, as the transmission provider's uses of its system.[72]

Refocusing the analysis was necessitated by the changing conditions in the electric utility industry, including the emergence of non-traditional suppliers and greater competition in bulk power markets. Because a transmission provider may use its system in different ways (e.g., to integrate load and resources when serving retail native load, to make off-system sales or purchases, or to serve wholesale requirements customers), the Commission set for hearing the factual issues associated with identifying those uses, as well as any potential impediments or consequences to providing comparable services to third parties.[73]

States Utilities Company v. FPC, 411 U.S. 747, 758-59 (1972)." *Id.* at p. 61,490 (footnote omitted). The Commission reaffirmed that it would examine how best to fulfill this responsibility, as well as its responsibility to prevent undue discrimination, in light of the changing conditions in the electric utility industry. *Id.*

[72]*Id.* at p. 61,490.

[73]*Id.* at pp. 61,490-91.

After AEP, the Commission applied this comparability standard to a proposed open access transmission tariff that was filed by Kansas City Power & Light Company (KCP&L) in support of a proposal to sell generation at market-based rates.[74] The Commission explained that, in light of AEP, the utility's proposed open access transmission tariff (which provided only **[31,648]** for point-to-point service) did not adequately mitigate its transmission market power so as to justify allowing the requested market-based rates. KCP&L could charge market-based rates for sales only if it modified its proposed transmission tariff to reflect the AEP comparability standard.

Since then, the Commission has required comparable service in a variety of contexts, and has set for hearing the factual issues associated with comparable service. For example, the Commission found that market power can be adequately mitigated only if a merged company offers transmission services in accordance with the AEP comparability standard.[75] The Commission further held that, even if a merger does not result in an increase in market power, the merger would not be consistent with the public interest under section 203 of the FPA unless the merged company offers comparable transmission services, as defined in AEP.[76] The Commission therefore announced a transmission comparability requirement for all new mergers:

---

[74]*See Kansas City Power & Light Company*, 67 FERC ¶61,183 (1994), *reh'g pending*.

[75]*E.g.*, *CSW*, *supra*, 68 FERC at p. 61,914.

[76]*Id.*

Given the transition of the electric utility industry as a whole, we conclude that, absent other compelling public interest considerations, coordination in the public interest can best be secured only if merging utilities offer comparable transmission services.[77]

In Heartland Energy Services, Inc.,[78] the Commission applied its comparability standard to an affiliated electric power marketer seeking blanket authorization to sell electricity at market-based rates. The Commission explained that

For all future cases involving blanket approval of market-based rates an offer of comparable transmission services will be required before the Commission will be able to find that transmission market power has been adequately mitigated. In the context of an affiliated power marketer, this means that all of its affiliated utilities must have a comparable transmission tariff on file.[79]

---

[77]*Id.* at p. 61,915 (footnote omitted).

[78]68 FERC ¶61,223 (1994).

[79]*Id.* at p. 62,060. In *InterCoast Power Marketing Company*, 68 FERC ¶61,248, *clarified*, 68 FERC ¶61,324 (1994), the Commission rejected an affiliated marketer's proposal to sell at market rates without its affiliate utility offering comparable transmission services. The Commission stated that the only way to ensure that InterCoast does not have transmission market power is to require its affiliated public utility to offer comparable transmission services. *See also LG&E Power Marketing Inc.*, 68 FERC ¶61,247 at pp. 62,120-21 (1994). The Commission added

The Commission also denied a request by a company affiliated with a transmission-owning utility seeking permission to sell power at market-based rates to a particular customer. The denial was without prejudice to refiling such a request in a new section 205 proceeding, but only after the affiliated transmission-owning utility filed a comparable transmission service tariff.[80] The Commission added that it

Will require comparability in any situation in which a seller seeking market-based rates is affiliated with an owner or controller of transmission facilities.[81]

The Commission has also stated that "it will henceforth apply the transmission comparability standard announced in the AEP case to all transmitting utility members of an RTG."[82]

---

that this is consistent with encouraging competitive bulk power markets as envisioned by the Energy Policy Act of 1992. *Id.* at p. 62,132.

[80]*See Hermiston Generating Company*, 69 FERC ¶61,035 at p. 61,164 (1994), *reh'g pending*. The Commission subsequently accepted the rates on a cost basis. See Letter Order dated November 10, 1994.

[81]*Id.* at p. 61,165.

[82]*See SWRTA*, 69 FERC at p. 61,397; *see also PacifiCorp, the California Municipal Utilities Association, and the Independent Energy Producers (on behalf of Western Regional Transmission Association)*, 69 FERC ¶61,099, *order on reh'g*, 69 FERC ¶61,352 (1994), *order on compliance filing*, 71 FERC ¶61,158 (1995) (*WRTA*). An RTG is a regional transmission group. It is defined as

[31,649]

The Commission further declared that comparable services must be provided through "open access" tariffs rather than only on a contract-by-contract basis:

(T)ariffs are essential to the provision of comparable services. Tariffs set out the services that are available and the terms and conditions under which those services will be made available * * *. (In contrast), a negotiation process creates uncertainty and imposes on customers delay and other transaction costs that the transmitting utility members of an RTG do not incur when using the transmission for their own benefit. Moreover, the ability to execute separate transmission agreements with different but similarly situated customers is the ability to unduly discriminate among them. A tariff ensures against such discrimination in the RTG.[83]

Thus, the Commission required the RTGs to amend their bylaws to commit all transmitting utility members to offer comparable transmission services to other RTG members pursuant to a transmission tariff or tariffs.

As discussed below, since the AEP comparability standard was announced, the Commission has set for hearing

---

"a voluntary organization of transmission owners, transmission users, and other entities interested in coordinating transmission planning (and expansion), operation and use on a regional (and inter-regional." Policy Statement Regarding Regional Transmission Groups, 58 FR 41626 (August 5, 1993), *FERC Statutes and Regulations* ¶30,976, at p. 30,870 n.4 (RTG Policy Statement).

[83]*SWRTA*, 69 FERC at p. 61,398.

44 open access tariffs to determine what constitutes comparable service. This number includes tariffs filed subsequent to the Open Access NOPR. All tariffs have now been made subject to the outcome of the Final Rule.

3. Lack of Market Power in New Generation

In 1994 in the KCP&L case, discussed in the prior section, the Commission continued to recognize that transmission remains a natural monopoly. However, it found that, in light of the industry and statutory changes that now allow ease of market entry, no wholesale seller of generation has market power in generation from new facilities.[84] In particular, the Commission explained that it had previously noted in Entergy Services, Inc. that

There was significant evidence that non-traditional power project developers, including qualifying facilities and independent power projects, are becoming viable competitors in long-run markets.[85]

The Commission further explained that since Entergy, Congress had enacted the Energy Policy Act, which had lowered barriers to the entry of new suppliers by creating a new class of power suppliers -- EWGs -- that are exempt from

---

[84]*KCP&L*, 67 FERC ¶61,183 (1994).

[85]*Id.* at p. 61,557 (citing *Entergy Services, Inc.*, 58 FERC ¶61,234 at p. 61,756 and nn.63 and 65 (*Entergy*)).

the provisions of PUHCA.[86] The Commission concluded that, in considering market-based rate proposals for generation sales, it need only focus on market power in transmission, generation market power in short-run markets, and other barriers to entry.[87]

4. Further Commission Action Addressing a More Competitive Electric Industry

To address the fact that the electric industry is becoming more competitive, and to remove barriers that might inhibit a more competitive industry, the Commission has initiated a number of proceedings: (1) Stranded Cost NOPR,[88] (2) Transmission Pricing Policy Statement,[89] (3) Pooling Notice of Inquiry,[90] (4) Regional Transmission Group

---

[86]*Id.* The Commission added that "after examining generation dominance in many different cases over the years, we have yet to find an instance of generation dominance in long-run bulk power markets." *Id.*

[87]*Id.*

[88]*FERC Statutes and Regulations* ¶32,507 (1994).

[89]Inquiry Concerning the Commission's Pricing Policy for Transmission Services Provided by Public Utilities Under the Federal Power Act, 59 FR 55031 (November 3, 1994), *FERC Statutes and Regulations* ¶31,005 (Transmission Pricing Policy Statement).

[90]Inquiry Concerning Alternative Power Pooling Institutions Under the Federal Power Act, 59 FR 54851 (October 26, 1994), *FERC Statutes and Regulations* ¶35,529 (1995) (Pooling Notice of

(RTG) Policy Statement,[91] and (5) Notice of Inquiry on Merger Policy.[92]

In the Stranded Cost NOPR the Commission recognized that the trend toward greater transmission access and the transition **[31,650]** to a fully competitive bulk power market could cause some utilities to incur stranded costs as wholesale requirements customers (or retail customers) use their supplier's transmission to purchase power elsewhere. As the Commission noted, a utility may have built facilities or entered into long-term fuel or purchased power supply contracts with the reasonable expectation that its customers would renew their contracts and would pay their share of long-term investments and other incurred costs. If the customer obtains another power supplier, the utility may have stranded costs. If the utility cannot locate an alternative buyer or somehow mitigate the stranded costs, the Commission explained that "the costs must be recovered from either the departing customer or the remaining customers or borne by the utility's shareholders."[93] Accordingly, the Commission proposed to establish provisions concerning the recovery of wholesale and retail stranded costs by public utilities and transmitting utilities.

Inquiry).

[91]*FERC Statutes and Regulations* ¶30,976 (RTG Policy Statement).

[92]*FERC Statutes and Regulations* ¶35,531 (1996).

[93]*FERC Statutes and Regulations* ¶32,507 at p. 32,864.

In the Transmission Pricing Policy Statement, the Commission announced a new policy providing greater flexibility in the pricing of transmission services provided by public utilities and transmitting utilities. The Commission traditionally had allowed only postage-stamp, contract-path pricing.[94] Under the new policy, we will permit a variety of proposals, including distance sensitive and flow-based pricing, which may be more suitable for competitive wholesale power markets.[95] The Commission explained that this "(g)reater pricing flexibility is appropriate in light of the significant competitive changes occurring in wholesale generation markets, and in light of our expanded wheeling authority

---

[94]Most transmission contracts set a single price for energy flow over a utility's transmission system. This single- price policy is called "postage stamp" pricing because the rate does not depend on how far the power moves within a company's transmission system. If power flows through several companies, traditional industry practice is to specify that power flows along a "contract path" consisting of the transmission-owning utilities between the ultimate receipt and delivery points. *See Indiana Michigan Power Company*, 64 FERC ¶61,184 at p. 62,545 (1993).

[95]Unlike with postage stamp pricing, with distance-sensitive pricing the cost of moving power through a company depends on how far the power moves within the company. In contrast to contract path pricing, flow-based pricing establishes a price based on the costs of the various parallel paths actually used when the power flows. Because flow-based pricing can account for all parallel paths used by the transaction, all transmission owners with facilities on any of the parallel paths could be compensated for the transaction.

under the Energy Policy Act of 1992."[96] However, the Commission explained that any new transmission pricing proposal must meet the Commission's AEP comparability standard. The Commission further explained that comparability of service applies to price as well as to terms and conditions.[97]

The Commission issued the Pooling Notice of Inquiry to receive comments on traditional power pools and on alternative power pooling institutions that are being explored in today's more competitive environment. The Commission expressed concern that

(G)iven the ongoing changes in the competitive environment of the electric utility industry -- in particular, the potential for substantially increased access to transmission -- we must consider whether we are appropriately balancing our dual objectives of promoting coordination and competition.[98]

Accordingly, the Commission explained that it wished to look at alternative power pooling institutions and to re-examine the role of more traditional power pools in today's environment of increased competition. In particular the Commission expressed its intent to ensure that its policies "are

---

[96]*FERC Statutes and Regulations* ¶31,005 at p. 31,136.

[97]*Id.* at p. 31,142.

[98]*FERC Statutes and Regulations* ¶35,529 at p. 35,715.

consistent with the development of a competitive bulk power market."[99]

In the RTG Policy Statement, the Commission announced a policy encouraging the development of RTGs. The Commission explained that a primary purpose of RTGs is to facilitate transmission access for potential users and voluntarily resolve **[31,651]** disputes over such service. The Commission has approved the formation of three RTGs.[100] One of the conditions is that each RTG member must offer comparable transmission services by tariff to other RTG members.

In the merger NOI, the Commission indicated that it will review whether its criteria and policy for evaluating mergers need to be modified in light of the changing circumstances occurring in the electric industry. In addition to the Commission's actions, a number of states have initiated proceedings concerning retail wheeling or proposed legislation for retail wheeling, that is, for ultimate consumers to choose their supplier of power, or other restructuring proposals.[101]

---

[99]*Id.* at p. 35,714. As explained below, the Commission held technical conferences on issues surrounding power pools and competition.

[100]*See WRTA* and *SWRTA*, *supra*, and *Northwest Regional Transmission Association*, 71 FERC ¶61,397 (1995).

[101]At least 12 states have retail wheeling proposals, legislation, or pilot programs underway -- Alabama, California, Connecticut, Illinois, Massachusetts, Michigan, New Hampshire, New York, Ohio, Rhode Island, Vermont, and Wisconsin. At least

5. Events Since Issuance of Open Access NOPR

Since issuance of the Open Access NOPR, public utilities have filed, in some form or another, 47 open access tariffs. In acting on those filings, the Commission has made all of the non- rate terms and conditions of those proposed tariffs subject to the outcome of this Final Rule.[102]

Over the last year, the Commission also has received and analyzed more than 20,000 pages of comments that were received from over 400 commenters, as well as additional information provided by industry participants at a number of Commission-initiated technical conferences.[103] Those technical

---

14 other states are investigating retail wheeling. Currently, according to a report of the NARUC-affiliated National Council on competition and the Electric Industry, 41 States are actively involved in investigating whether and how to restructure their respective electric power markets. Of this total, 29 State regulatory authorities * * * have initiated investigations. In addition, five State legislatures are involved in similar investigations, while seven other States have joint regulatory/legislative proceedings underway.

Testimony of the Honorable Cheryl L. Parrino, Chair of the Wisconsin Public Service Commission, on behalf of the National Association of Regulatory Utility Commissioners, before the United States Senate Committee on Energy and Natural Resources (March 6, 1996).

[102]*See American Electric Power Service Corporation*, et al., 72 FERC ¶61,287 at p. 61,238 (1995).

[103]Attached to this Final Rule as Appendix B is a list of commenters and the abbreviations used to designate them, including

conferences addressed several issues -- ancillary services, pro forma tariffs, power pools, and ISOs -- and provided significant input to the Commission's formulation of this Final Rule.

F. *Need for Reform*

The many changes discussed above have converged to create a situation in which new generating capacity can be built and operated at prices substantially lower than many utilities' embedded costs of generation. As discussed above, new generation facilities can produce power on the grid at a cost of less than 3 cents per kWh to 5 cents per kWh, yet the costs for large plants constructed and installed over the last decade were typically in the range of 4 to 7 cents per kWh for coal plants and 9 to 15 cents for nuclear plants.

Non-traditional generators are taking advantage of this opportunity to compete. Indeed, the non-traditional generators' share of total U.S. electricity generation increased from 4 percent in 1985 to 10 percent in 1993.[104] Much of this increased share of generation is the result of competitive bidding for new generation resources that has occurred in 37 states. Since 1984, almost 4,000 projects, representing over 400,000 MW, have been offered in response to requests. Over 350 projects have been selected to supply 20,000 MW, and,

---

those commenters that filed late.

[104]Energy Information Administration, *Performance Issues for a Changing Electric Power Industry* (January 1995) 10 and (Figure 5).

of these, 126 are now online producing almost 7,800 MW of power.[105]

In addition, the cost of utility-generated electricity differs widely across the major regions of the United States. Average utility rates range from 3 to 5 cents in the Northwest to 9 to 11 cents in California. **[31,652]** Electricity consumers are demanding access to lower cost supplies available in other regions of the United States, and access to the newer, lower cost generation resources. Therefore, it is important that the non-traditional generators of cheaper power be able to gain access to the transmission grid on a non-discriminatory open access basis.

The Commission's goal is to ensure that customers have the benefits of competitively priced generation. However, we must do so without abandoning our traditional obligation to ensure that utilities have a fair opportunity to recover prudently incurred costs and that they maintain power supply reliability. As well, the benefits of competition should not come at the expense of other customers. The Commission believes that requiring utilities to provide non-discriminatory open access transmission tariffs, while simultaneously resolving the extremely difficult issue of recovery of transition costs (discussed infra), is the key to reconciling these competing demands.

Non-discriminatory open access to transmission services is critical to the full development of competitive

---

[105]Current Competition, November 1994, Vol. 5, No. 8, at p. 8.

wholesale generation markets and the lower consumer prices achievable through such competition.[106] Transmitting utilities own the transportation system over which bulk power competition occurs and transmission service continues to be a natural monopoly. Denials of access (whether they are blatant or subtle), and the potential for future denials of access, require the Commission to revisit and reform its regulation of transmission in interstate commerce. As discussed in detail in Section IV.B., such action is required by the FPA's mandate that the Commission remedy undue discrimination.

Since the time the NOPR issued, the Commission staff has completed an FEIS that provides a quantitative estimate of some of the cost savings expected from this Rule: approximately $3.8 to $5.4 billion per year. Other non-quantifiable benefits are also expected from this Rule and include: (1) better use of existing assets and institutions; (2) new market mechanisms; (3) technical innovation; and (4) less rate distortion. These potential benefits to the Nation's electricity consumers and the economy as a whole confirm the need to take generic action to remove barriers to competition. In what follows, we set out the changes necessary to remedy undue discrimination and to ensure a fair transition to a more competitive regulatory regime.

---

[106]As discussed above, a significant number of public utilities still do not have any form of an "open access" tariff on file with the Commission and no public utility has on file a non-discriminatory open access tariff as defined by this Rule.

IV. Discussion

A. *Scope of the Rule*

1. Introduction

The Commission has determined that non-discriminatory open access transmission services (including access to transmission information) and stranded cost recovery are the most critical components of a successful transition to competitive wholesale electricity markets. These issues are the focal point of this Rule, the accompanying rule on open access same-time information systems, and the accompanying proposed rule on capacity reservation tariffs.

In undertaking these initiatives, however, we are mindful that they are part of a broader picture of evolving issues affecting the electric industry and that other Commission policies will play an important role in ensuring the full development of competitive markets. Among the many issues that are important to competitive bulk power markets are: independent system operators (ISOs); regional transmission groups; generation market power; utility merger policy; and the development of innovative transmission pricing alternatives, such as flow-based, distance-sensitive transmission pricing methodologies that reflect incremental costs. In particular, we believe that ISOs have great potential to assist us and the industry to help provide regional efficiencies, to facilitate economically efficient pricing, and, especially in the context of power pools, to remedy undue discrimination and mitigate market power. Although we discuss some of these issues in this Rule, we will further

develop our policies in other proceedings as well to accommodate and encourage more efficient market structures.

[31,653]

We now address the comments received on the scope of the proposed rulemaking.

2. Functional Unbundling

In the NOPR, the Commission preliminarily found that functional unbundling of wholesale generation and transmission services is necessary to implement non-discriminatory open access transmission.[107] At the same time, the Commission explained that the proposed rule would accommodate, but not require, corporate unbundling (which could include selling generation or transmission assets to a non-affiliate (divestiture) or the less aggressive step of establishing separate corporate affiliates to manage a utility's transmission and generation assets). However, we invited comments on functional unbundling and asked whether it is a strong enough measure to ensure non-discriminatory open access transmission without some form of corporate restructuring.

Comments

Commenters take both sides on whether functional unbundling is sufficient to assure non-discriminatory open access transmission or whether a stronger measure, such as

---

[107] *FERC Statutes and Regulations* ¶32,514, at p. 33,080.

corporate unbundling, is needed. Supporting functional unbundling

Various commenters, including utilities and state commissions, generally support functional unbundling as sufficient to assure non-discriminatory open access transmission and oppose requiring corporate unbundling or divestiture.[108] Several commenters state that functional unbundling will remedy discrimination without creating the inefficiencies and additional costs that corporate restructuring would create.[109]

A number of other commenters argue that the Commission has no authority under the FPA to require divestiture of transmission assets.[110] Several of these commenters assert that, even if the Commission has the authority, the electric industry, unlike the natural gas industry, is not ready for mandated corporate unbundling because electric utilities still serve a high percentage of retail customers and own large amounts of the generating capacity.

---

[108]*E.g.*, Ohio Edison, UtiliCorp, Pennsylvania P&L, Atlantic City, Montana Power, IL Com, Seattle, OK Com, TX Industrials, MidAmerican, Southwestern, Southern, DOD, Public Service Co of CO, SC Public Service Authority, Florida Power Corp, DOE, WP&L, Com Ed, SBA, Consumers Power, CA Com, UT Com, Houston L&P, KCPL, EEI.

[109]*E.g.*, Florida Power Corp, El Paso, PSNM, and SC Public Service Authority.

[110]*E.g.*, Southwestern, PECO, El Paso, Florida Power Corp, NSP, Public Service E&G, MidAmerican.

They assert that transmission system operation requires the operator to have control over much of the generating capacity.

Various other commenters also support functional unbundling, but believe that safeguards are needed to make it work.[111] Power Marketing Association, for example, suggests a number of safeguards: adoption of cost allocation mechanisms to ensure that utilities do not shift costs from generation to transmission; random audits of utility books; a requirement that each utility file a code of conduct that provides for maximum separation of generation and transmission functions; and active oversight and complaint procedures with strong penalties for abuse. OK Com and GA Com believe that functional unbundling along with the safeguard of the Commission's complaint process will provide sufficient incentive for non-discriminatory open access transmission.

Supporting Corporate Unbundling

A number of commenters see weaknesses in functional unbundling and argue that some form of corporate unbundling is necessary to assure non-discriminatory open access transmission.[112] American Forest & Paper says that there is

---

[111]*E.g.*, NRECA, IN Com, Power Marketing Association, TDU Systems, NorAm, Turlock, Texaco, Utility Shareholders, NSP, El Paso, Utility Investors Analysts, PECO, Florida Power Corp, UT Com, Sierra, Carolina P&L, SoCal Gas, OK Com, FL Com, Southern.

[112]*E.g.*, American Forest & Power, American National Power, ND Com, IL Com, UAMPS, NIEP, APPA, Public Power

affiliate abuse in the gas industry and argues that **[31,654]** the electric industry presents even more serious potential for abuse because it is still dominated by vertically integrated utilities.[113] UAMPS asserts that functional unbundling is insufficient because the utility will still favor itself on issues related to transmission planning, capital investment, and operation and maintenance and replacement costs.

NIEP argues that divestiture of generation assets from transmission and distribution is the preferred mechanism for mitigating market power. It further suggests that if corporate divestiture is not feasible the Commission should

Seek to achieve "virtual divestiture" by requiring that the utility generation function be separated from transmission and distribution functions in a separate corporate affiliate, or business unit, and that affiliate transaction rules be established to guard against possible abuses.[114]

It maintains that the Commission has broad authority to protect against undue discrimination and anticompetitive

---

Council, Municipal Energy Agency Nebraska, Missouri Basin MPA, Texaco, Direct Services Industries, Calpine, CCEM, Wisconsin Coalition, VT DPS.

[113]*See also* American National Power, ND Com, Calpine.

[114]NIEP Initial Comments at p. 4.

behavior and can order divestiture if such action is required to remedy such behavior.[115]

FTC and DOJ argue that operational unbundling, an example of which is the formation of an independent system operator (ISO), likely would be more effective than functional unbundling and less costly than industry-wide divestiture.[116] FTC describes operational unbundling as "structural institutional arrangements, short of divestiture, that would separate operation of the transmission grid and access to it from economic interests in generation." It gives as an example the California proposal under which utilities would continue to own transmission lines, but an independent system operator would have operational control. DOJ also suggests "a separate authority" to manage the grid and access to the grid, joint ventures, and voluntary pooling arrangements. These commenters argue that operational unbundling would be easier to enforce than functional unbundling.

DOE states that separation of the control of transmission from vertically-integrated companies does not necessarily require a poolco or any particular market mechanism. It suggests the possibility of an ISO that is functionally separate from any buyer or seller of generation, but would not perform all the functions of a poolco.

---

[115]*See also* Municipal Energy Agency Nebraska, Direct Services Industries.

[116]Others oppose operational unbundling. *See, e.g.*, Carolina P&L, Salt River.

United Illuminating supports "operational unbundling" that would either (1) eliminate vertical integration and divestiture of transmission assets, leading to the formation of a regional transmission company, or (2) develop a regional contractual approach to transmission services that eliminates the transmission owner's market power and fairly allocates support of the transmission facilities between native load and third-party users of the system. Commission Conclusion

We conclude that functional unbundling of wholesale services is necessary to implement non-discriminatory open access transmission and that corporate unbundling should not now be required. As we explained in the NOPR, functional unbundling means three things:

(1) A public utility must take transmission services (including ancillary services) for all of its new wholesale sales and purchases of energy under the same tariff of general applicability as do others;

(2) A public utility must state separate rates for wholesale generation, transmission, and ancillary services;

(3) A public utility must rely on the same electronic information network that its transmission customers rely on to obtain information about its transmission system when buying or selling power.

We believe that these requirements are necessary to ensure that public utilities provide non-discriminatory

service.[117] These requirements also will give public **[31,655]** utilities an incentive to file fair and efficient rates, terms, and conditions, since they will be subject to those same rates, terms, and conditions.

However, we recognize that additional safeguards are necessary to protect against market power abuses. Functional unbundling will work only if a strong code of conduct (including a requirement to separate employees involved in transmission functions from those involved in wholesale power merchant functions) is in place. In the RINs NOPR, the Commission proposed a code of conduct that would apply to all public utility transmission providers. As the Commission explained,

> [T]his code of conduct would require, among other matters, a separation of the utilities' transmission system operations and wholesale marketing functions, and would define permissible and impermissible contacts between employees that conduct wholesale generation marketing functions and employees that handle transmission system operations and reliability in the system control center or at other facilities or locations.[118]

---

[117]When and how functional unbundling is to be achieved for requirements transactions and for various types of coordination arrangements, including power pools, is discussed at Sections IV.A.5 and IV.F. Functional unbundling of ancillary services is discussed in Section IV.D.

[118]Real-Time Information Networks and Standards of Conduct, Notice of Proposed Rulemaking, 60 FR 66182 (December 21, 1995), *FERC Statutes and Regulations* ¶32,516 at p. 33,170

Adoption of this code of conduct, discussed in detail in the accompanying final rule on OASIS,[119] is needed to ensure that the transmission owner's wholesale marketing personnel and the transmission customer's marketing personnel have comparable access to information about the transmission system.

As noted by OK Com and GA Com, a further safeguard -- section 206 -- is available if a public utility seeks to circumvent the functional unbundling requirements. Under section 206, any person is free to file a complaint with the Commission detailing any alleged misbehavior on the part of the public utility or its affiliates concerning matters subject to our jurisdiction under the FPA. Similarly, the Commission may, on its own motion, initiate a proceeding to investigate the practices of the public utility and its affiliates.

We believe that functional unbundling, coupled with these safeguards, is a reasonable and workable means of assuring that non-discriminatory open access transmission occurs. In the absence of evidence that functional unbundling will not work, we are not prepared to adopt a more intrusive and potentially more costly mechanism -- corporate unbundling -- at this time.

(1995).

[119]The final rule on information systems no longer uses the terminology RINs. The new terminology used is OASIS -- Open Access Same-time Information System -- which we will use in this Final Rule.

Several commenters discuss the need to encourage or even to require ISOs in the context of functional unbundling. We believe that ISOs have the potential to provide significant benefits (e.g., to help provide regional efficiencies, to facilitate economically efficient pricing, and, especially in the context of power pools, to remedy undue discrimination and mitigate market power) and will further our goal of achieving a workably competitive market. As we learned at our technical conference on power pools, many utilities are examining ISOs and corporate unbundling in various shapes and forms, particularly in the context of power pools. We discuss ISOs extensively in our section on power pools where we believe they will have an important role to play. However, in the context of individual utility transactions, we believe that the less intrusive functional unbundling approach outlined above is all that we must require at this time. Nevertheless, we see many benefits in ISOs, and encourage utilities to consider ISOs as a tool to meet the demands of the competitive marketplace.

As a further precaution against discriminatory behavior, we will continue to monitor electricity markets to ensure that functional unbundling adequately protects transmission customers. At the same time, we will analyze all alternative proposals, including formation of ISOs, and, if it becomes apparent that functional unbundling is inadequate or unworkable in assuring non-discriminatory open access transmission, we will reevaluate our position and decide whether other mechanisms, such as ISOs, should be required.

Finally, while we are not now requiring any form of corporate unbundling, we again encourage utilities to explore whether corporate unbundling or other restructuring **[31,656]**

mechanisms may be appropriate in particular circumstances. Thus, we intend to accommodate other mechanisms that public utilities may submit, including voluntary corporate restructurings (e.g., ISOs, separate corporate divisions, divestiture, poolcos), to ensure that open access transmission occurs on a non-discriminatory basis. We also will continue to monitor -- and stand ready to work with parties engaging in -- innovative restructuring proposals occurring around the country.

3. Market-Based Rates

a. Market-Based Rates for New Generation

In the NOPR, the Commission proposed to codify its determination in Kansas City Power & Light Company[120] that the generation dominance standard for market-based sales from new capacity be dropped.[121] The proposed new section 35.27 would provide:

Notwithstanding any other requirements, any public utility seeking authorization to engage in sales for resale of electric energy at market-based rates shall not be required to demonstrate any lack of market power in generation with respect to sales from capacity first placed in service on or after June 10, 1996.[122]

---

[120]67 FERC ¶61,183 at p. 61,557 (1994), *reh'g pending* (KCP&L).

[121]*FERC Statutes and Regulations* ¶32,514 at p. 33,050.

[122]*Id.* at p. 33,154.

However, this proposal would not affect the Commission's continuing authority to look at whether an applicant and its affiliates could erect other barriers to entry and whether there may be affiliate abuse or reciprocal dealing.[123]

Comments

A number of commenters support the Commission's determination in KCP&L[124] and several of them explicitly support the Commission's proposed codification.[125] EEI asserts that more than 50 percent of new generation is from non-utility sources and that recent competitive solicitations for new capacity have been greatly over-subscribed. Entergy argues that there is no evidence in any proceeding thus far of a market power problem in long-run markets.

Other commenters, however, oppose codifying KCP&L.[126] They believe that market power in long-run markets exists for both new and old generation due to, for example, constraints on interface capabilities and unduly long notice periods for replacement of purchases. They argue that

---

[123]67 FERC at p. 61,557.

[124]*E.g.*, Entergy, EEI, Atlantic City, Duke Centerior, Houston L&P, Montana-Dakota Utilities, Canadian Petroleum Producers, DOE, Florida Power Corp, PSNM.

[125]*E.g.*, EEI, Centerior, Houston L&P, NYSEG.

[126]*E.g.*, TDU Systems, ELCON, NRECA, Environmental Action, NIEP, APPA, Power Marketing Association, EGA.

there is not enough of a distinction between new and old generation to treat them differently. TDU Systems also notes that the Commission in KCP&L did not take into account the differences between firm and non- firm bulk power. NIEP and ELCON conclude that the Commission erroneously found in KCP&L that no wholesale seller of generation has market power in generation from new facilities. NIEP asserts that in each service area there is usually only one wholesale buyer -- the utility -- who also is virtually always a wholesale seller of generation. Under these circumstances, NIEP argues that there cannot be arm's-length bargaining. Environmental Action complains that the Commission's proposal to codify KCP&L ignores significant factors that impede entry to generation markets, such as utility resistance to purchased power, state government-created barriers to non-utility generation, pancaking of rates under the contract path approach, sunk investment, and scale economies.

Commission Conclusion

In reviewing applications to sell at market-based rates, whether from new (unbuilt) capacity or existing capacity, we require that the seller (and each of its affiliates) must not have, or must have mitigated, market power in generation and transmission and not control other barriers to entry. In order to demonstrate the requisite absence or mitigation of transmission market power, a transmission-owning public utility seeking to sell at market-based rates must have on file **[31,657]** with the Commission an open access transmission tariff for the provision of comparable service. In addition, the

Commission considers whether there is evidence of affiliate abuse or reciprocal dealing.[127]

In KCP&L, we stated that "in light of industry and statutory changes which allow ease of market entry, we therefore will no longer require rate applicants to submit evidence of generation dominance in long-run bulk power markets."[128] We further explained that we had examined "generation dominance in many different cases over the years" and had "yet to find an instance of generation dominance in long-run bulk power markets."[129] Commenters have criticized our findings in KCP&L, but no commenter has provided any evidence of generation dominance in long-run bulk power markets. Moreover, we have seen no such evidence in any of the market-based rate cases we have considered since KCP&L. Based on the comments received, we will codify the Commission's determination in KCP&L that the generation dominance standard for market-based sales from new capacity should be dropped. Because the Commission's findings in KCP&L applied to long-run markets, we will revise proposed §35.27 to apply to sales

---

[127]*See, e.g., MidAmerican Energy Company*, 74 FERC ¶61,211 (1996).

[128]*KCP&L*, 67 FERC at p. 61,557. *See also* discussion in proposed rule, *FERC Statutes and Regulations* at pp. 33,067-68.

[129]*Id.*

from capacity for which construction has commenced on or after the effective date of this Rule.[130]

The Commission wishes to clarify that dropping the generation dominance standard for new capacity does not affect the demonstration that an applicant must make in order to qualify for market-based rates for sales from its existing generating capacity. In other words, the fact that an applicant need not demonstrate its lack of generation dominance with respect to new capacity cannot be used to "bootstrap" the authorization of market-based rates for its existing capacity. Moreover, our evaluation of market-based rates for existing capacity will include consideration of new capacity.

In addition, the fact that we are codifying KCP&L does not mean that we will ignore specific evidence presented by an intervenor that a seller requesting market-based rates for sales from new generation nevertheless possesses generation dominance. For example, if the evidence indicated that the new generator, due to its proximity to an existing transmission constraint, could significantly influence the ability to move power across the constraint, we would consider such evidence in determining whether to grant the

---

[130]The NOPR's proposed language that a public utility would not have to demonstrate a lack of market power in generation for sales from capacity first placed in service on or after the date 30 days after the final rule is published in the *Federal Register* does not properly reflect the finding in *KCP&L*. Because *KCP&L* addressed new or unbuilt generation, the proposed language is being revised as indicated above and as set forth in the regulatory text included with this Final Rule.

applicant's request.[131] If such evidence is presented, the Commission will evaluate whether the evidence disproves the premise that the seller lacks generation dominance with respect to its new capacity.

If the applicant has existing generation, the sales from which are authorized to be made on a market basis, the Commission would consider whether the new generation (when added to the existing generation with market-based authority) results in the applicant having generation dominance. On the other hand, if the applicant has existing generation, the sales from which are subject to cost-of-service regulation, the Commission would not include this generation in its analysis of the applicant's request for market-based rates for its new generation. The question of whether or not the applicant lacks generation dominance with respect to its existing capacity is relevant only if, and when, the seller applies to the Commission for authority to make wholesale sales for its existing capacity at market-based rates.

If evidence regarding an applicant's generation dominance with respect to its new capacity is submitted, the applicant would be required to provide a satisfactory rebuttal.

[31,658]

b. Market-Based Rates for Existing Generation

In the NOPR, the Commission explained that increased competition resulting from open access transmission may

---

[131]*Cf. Wisconsin Electric Power Company, et al.*, 74 FERC ¶61,069 at p. 61,193 (1996).

reduce or even eliminate generation-related market power in the short-run market (sales from existing capacity).[132] Because market power has been the primary concern of the Commission in analyzing requests for market-based rates for such sales, we sought comments on the effect of industry-wide non-discriminatory open access on our criteria for authorizing power sales at market- based rates. The Commission also sought comments on whether the generation dominance standard should be dropped for market-based sales from existing capacity.

Comments

Many commenters support, but many also oppose, market-based rates for existing generation without a case-specific analysis of generation dominance.

Supporting Market-Based Rates for Existing Generation.

Many commenters (primarily IOUs and a number of state commissions) assert that existing generators will not possess market power after implementation of non-discriminatory open access transmission and that market-based rates should be permitted generically for sales from existing generation.[133]

---

[132]*FERC Statutes and Regulations* ¶32,514, at pp. 33,093-94.

[133]*E.g.*, EEI, CINergy, Central Illinois Public Service, Citizens Utilities, Com Ed, Ohio Edison, Allegheny, Southern, Portland, NRRI, Pennsylvania P&L, PECO, Dayton P&L, Utilities For Improved Transition, Centerior, Houston L&P, Duke, ConEd,

EEI asserts that market power concerns generally would be transitory, limited to the time needed to build new facilities. Thus, it recommends that all markets be declared competitive by a date certain and that market-based rates then be allowed, with customers permitted to file complaints. Florida Power Corp believes that existing procedures under sections 205 and 206 will adequately protect consumers. Other commenters also urge the Commission to eliminate its generation dominance standard, but assert that the Commission should allow a showing of market dominance in a complaint or show cause proceeding.[134] CT DPUC notes that the Commission should be able to rely on rules of conduct, market mechanisms, and monitoring to curb any market power that may exist.

Utilities For Improved Transition argues that if utilities cannot get market-based rates, the new players in the market will have an unfair advantage, since they do not have to carry the traditional utilities' burden of older, less efficient plants.

Entergy proposes a screening test that would permit the Commission to "deregulate" wholesale sales to certain short-run markets. CINergy recommends that after industry-wide open access tariffs become effective, the Commission adopt a rebuttable presumption that all markets are workably

---

IPALCO, Salt River, PJM, NU, NYSEG, Oklahoma G&E, PA Com, OK Com, CT DPUC, CA Com, MT Com.

[134]*E.g.*, Consumers Power, Portland, Dayton P&L, CSW.

competitive; that presumption could be rebutted in a section 206 proceeding.[135]

UtiliCorp, while it believes that market power will probably be fully mitigated by open access, also argues that the Commission should examine generation dominance on a region-by-region basis.[136] Montana-Dakota Utilities argues that the Commission should allow all suppliers in a power pool or RTG to have market-based rates after a Commission finding that there is sufficient generation competition within the region.

Duke states that it would be highly inconsistent for the Commission to require open access, but not allow utilities to compete in the market. It further states that the relevant market should be determined using standard antitrust techniques; the Commission should examine the options available to customers and determine whether the utility possesses monopoly power in a relevant market.

[31,659]
Opposing Market-Based Rates for Existing Generation

Many commenters are concerned that even with open access tariffs certain generators will be able to exercise

---

[135]*See also* Citizens Utilities.

[136]*See also* CSW, Industrial Energy Applications, Public Service Co of CO, Coalition for Economic Competition.

market dominance.[137] For example, NARUC argues that utilities retain market power through their ownership of existing generation and transmission facilities, favorable long-term contracts for fuel and other inputs, and access to superior generation sites.[138] NRECA believes that the universe of generation providers is still too narrow to assume a competitive market and that other factors, such as transmission constraints and pancaking of rates, will inhibit the development of competitive markets.[139] FTC says that, although comparable transmission access could broaden the relevant geographic market for generation, the Commission should not assume that there will be no market power. It says that the Commission must continue to evaluate each case.[140]

---

[137]*E.g.*, NRECA, TDU Systems, MT Com, SMUD, NEPCO, Orange & Rockland, El Paso, American Forest & Paper, NIPSCO, AEC & SMEPA, OH Com, IL Com, IN Com, Legal Environmental Assistance, LG&E, Cajun, Industrial Energy Applications, LEPA, MA DPU, MI Com, FTC, Minnesota P&L, SC Public Service Authority, WP&L, NARUC, Canadian Petroleum Producers, DOD, CCEM, Environmental Action, American Wind, Cajun, NIEP, EGA, TAPS, ELCON, Consolidated Natural Gas.

[138]*See also* NIEP, Pacificorp, CA Energy Com.

[139]*See also* MT Com, TDU Systems, Soyland.

[140]*See also* AEC & SMEPA, NIPSCO, El Paso (discusses a particular transmission constraint that it states limits its access to suppliers).

NRECA is also concerned that mergers may create a handful of "mega-public utilities" that may affect a regional

TDU Systems argues that the Commission cannot move to market-based rates without a Congressional determination that deregulation of wholesale electric rates should be implemented. It further asserts that the Commission does not have a factual basis for a reasoned conclusion that regulated utilities do not have market dominance -- full open access is only a goal at this time, and the success of open access will depend upon the transmission rate structures the Commission approves.

LEPA raises concerns that the small bulk power suppliers, QFs, co-generators, EWGs, IPPs, and marketers (who provide non- requirements power) may not be able to bring competition to the wholesale market. LEPA concludes that "barriers will exist unless buyers have full access to requirements power itself, rather than just to the chance to acquire the individual components of requirements power."[141] TDU Systems raises concerns about the limited number of generation providers and the effect of possible future mergers. It also argues that pancaked rates raise the cost of transmission to third parties, thereby restricting the geographic scope of markets. As a result, TDU Systems asserts that individual generators in highly concentrated regions will still be able to exert market power. OH Com expresses concerns that restrictions on siting of generation and transmission will favor nearby generators. SC Public Service

---

generation market and that the Commission should apply more traditional antitrust principles in analyzing the impacts of mergers.

[141]LEPA Initial Comments Affidavit of William G. Shepherd at p. 4.

Authority argues that if the Commission allows utilities to recover stranded costs their market power will not be mitigated, since customers will have to pay exit fees to switch suppliers.[142]

CCEM notes that in Order No. 636 gas pipelines were not allowed market-based rates for merchant sales until after transmission had been completely unbundled and non-discriminatory open access had been fully implemented.

DOE and DOJ assert that open access should not be assumed to mitigate market power sufficiently to justify deregulation of existing generation -- structural changes, such as control of the regional grid by an independent entity, are required. DOE requests that the Commission continue to look for affiliate abuse when reviewing market-based rates for new generation. Similarly, EPA is concerned that even with open access, individual generators may still exert market power by their domination of a particular geographic market. It is also concerned **[31,660]** that low-cost plants that are subject to weaker environmental standards could have a market advantage. NEPOOL Review Committee requests that the Commission not approve any market prices "where the market into which the seller proposes to sell is not effectively competitive due to the absence of regional transmission products and prices."[143]

---

[142]*See also* DOD and WP&L. IL Com suggests that the Commission allow market-based rates to a utility on the condition that the utility forego stranded cost recovery.

[143]NEPOOL Review Committee Initial Comments at p. 28.

Commission Conclusion

While the Commission expects this Rule to facilitate the development of competitive bulk power markets, we find that there is not enough evidence on the record to make a generic determination about whether market power may exist for sales from existing generation. We continue to have concerns about how to define the relevant markets and believe that a more rigorous analysis is needed than can be achieved with the limited market data that is now available. We will continue our case-by-case approach that allows market-based rates based on an analysis of generation market power in first tier and second tier markets.[144] In particular cases, however, the effect of the mandatory open access prescribed by this Final Rule may lead to the consideration of geographic markets for the applicant's generation products that are broader in scope than the first-tier and second-tier markets currently considered.[145] By the same token, in some cases,

---

[144]*See, e.g., Southwestern Public Service Company*, 72 FERC ¶61,208 at p. 61,996 (1995).

[145]The Commission's practice is to define the relevant markets as those utilities directly interconnected to the applicant (first-tier markets). For each first-tier market, we consider all utilities interconnected to the first-tier utility and all utilities interconnected to the applicant as competitors in that relevant market. Thus, the competitors include the second-tier utilities directly interconnected to the relevant market and those other first-tier utilities that can reach the market by virtue of the applicant's open access transmission tariff. *See, e.g., Kansas City Power & Light Company*, 67 FERC ¶61,183 at p. 61,556; and *Heartland Energy Services, Inc.*, 68 FERC ¶61,223 at p. 62,061.

evidence of the effects of transmission constraints may circumscribe the scope of the relevant geographic market for the applicant's generation products.

While we will continue to apply the first-tier/second-tier analysis, we will allow applicants and intervenors to challenge the presumption implicit in the Commission's practice that the relevant geographic market is bounded by the second-tier utilities. Thus, for instance, applicants may present evidence that the relevant market is in fact broader than the first or second tier. In support of such a contention, an applicant would need to show more than the existence of open access. For example, an applicant might attempt to demonstrate the lack of significant transmission constraints in the more broadly defined market and that cumulative transmission rates would not significantly affect the ability of more distant suppliers to compete in the relevant market. Similarly, an intervenor may present evidence that, due to the existence of significant transmission constraints within the first- and second-tier markets, the relevant market is in fact more limited in scope.[146]

Finally, we will maintain our current practice of allowing market-based rates for existing generation to go into effect subject to refund. To the extent that either the applicant or intervenors in individual cases offer specific evidence that the relevant geographic market ought to be defined differently than under the existing test, we will examine such arguments through formal or paper hearings.

---

[146]*See Wisconsin Public Service Corporation*, 75 FERC ¶61, --, slip op. at pp. 6-7 (1996).

Because our goal is to develop more competitive bulk power markets, we will continue to monitor markets to assess the competitiveness of the market in existing generation, and we will modify our market rate criteria if and when appropriate. However, any changes we might make to our analysis for authorizing market-based rates in the future will not upset transactions entered into pursuant to existing market-based rate authority. The policies we put in place today to develop a smoothly functioning transmission access regime will provide useful experience and information for assessing the effects of generation concentration.

4. Merger Policy

In the NOPR, the Commission did not address possible ramifications of the **[31,661]** NOPR with regard to its existing merger policy.

Comments

A number of commenters suggest that the Commission should reevaluate its merger policy in light of the NOPR.[147] They further suggest a number of changes that they believe need to be made to the Commission's existing merger policy.

Most commenters raising this issue express concerns that mergers will lessen competition and hinder achievement of competitive bulk power markets.[148] For example, NRECA

---

[147]*E.g.*, NRECA, TAPS, Wisconsin Coalition, APPA.

[148]*E.g.*, Wisconsin, Rosebud, NRECA, IN Com, Wisconsin Coalition, NIEP, Minnesota P&L, APPA.

indicates that the Commission's merger policy is at a crossroads. It believes that it is essential for the Commission to reevaluate its merger policy in concert with the proposed rulemakings.[149] Similarly, TAPS recommends that the Commission reevaluate its merger criteria to ensure that in a more competitive era, mergers are found to be consistent with the public interest only if they are pro-competitive. Several commenters argue that the Commission should continue to conduct a case-by-case investigation of the product and geographic markets that will be affected by a proposed merger.[150]

A number of commenters also suggest certain changes that they would like to see in the Commission's merger policy.[151] APPA recommends that, at a minimum, all merger approvals considered by the Commission should be conditioned on: (1) filing an open access transmission tariff, (2) demonstrating no market power in generation or ancillary services, and (3) granting all existing requirements customers of the merged entity the right to convert existing contracts to rights to equivalent transmission capacity. Several commenters suggest adopting the U.S. Department of Justice Merger Guidelines in analyzing merger proposals.[152]

---

[149]*See also* APPA.

[150]*E.g.*, Wisconsin Coalition, MMWEC.

[151]*E.g.*, APPA, Wisconsin Coalition, Minnesota P&L, IN Com.

[152]*E.g.*, Wisconsin Coalition.

Environmental Action and others contend that merging utilities must be required to demonstrate real net benefits to retail and wholesale customers that could not otherwise be achieved but for the proposed merger.[153]

Commenters also argue that the Commission should use its merger conditioning authority to order divestiture of transmission and generation when required to ensure competition.[154] Environmental Action and NEPOOL Review Committee suggest conditioning merger applications on the existence of regional transmission pricing arrangements to mitigate any generation market power gained by the merging entities.

Commission Conclusion

The Commission appreciates the concerns and suggestions raised with respect to our merger policy. However, since the time the NOPR was issued (and comments received thereon), we issued a Notice of Inquiry on the Commission's merger policy in Docket No. RM96-6-000.[155] There we indicated that we will review whether our criteria and policies for evaluating mergers need to be modified in light of the changing circumstances, including this final rule, that are occurring in the electric industry. The NOI proceeding will permit us to consider comments from all

---

[153]E.g., TAPS, Wisconsin Coalition.

[154]*E.g.*, NIEP, Wisconsin Coalition, TAPS, Environmental Action.

[155]*FERC Statutes and Regulations* ¶35,531 (1996).

interested participants and, at the same time, allow us to review our merger criteria and policies in light of this final rule. We are committed to reviewing our merger policy in a timely manner in the ongoing NOI proceeding.[156]

5. Contract Reform

In the NOPR, the Commission explained that it believed that it could remedy unduly discriminatory practices and achieve more competitive bulk power markets without abrogating existing **[31,662]** wholesale power supply contracts that bundle generation and transmission services and existing wholesale transmission contracts.[157] Thus, we proposed to apply the functional unbundling requirement only to transmission services under new requirements contracts, new coordination contracts, and new transactions under existing coordination contracts. However, the Commission did invite comment on whether it would be contrary to the public interest to allow all or some of the above types of existing contracts to remain in effect.

---

[156]Our decision to review our merger policy in a separate NOI proceeding is not intended to affect a utility's business decision of whether a merger may be in the economic interest of its ratepayers and stockholders. The NOI proceeding will not prevent us from reviewing merger applications in as timely a manner as possible.

[157]*FERC Statutes and Regulations* ¶32,514 at p. 33,093.

Requirements and Transmission Contracts

Many of the commenters (including utility customers and third-party power suppliers) addressing this issue oppose abrogating existing contracts on a generic basis.[158] A number of the commenters contend that existing contracts should be retained because they are the result of mutually beneficial bargaining.[159] SMUD and TANC are concerned that existing contracts providing for transmission service that is superior to the pro forma tariffs not be abrogated.[160] Ohio Edison argues that existing contracts have contributed to the emergence of competition, meet the specific needs of the parties, have been approved by the Commission, and have not been found to be unduly discriminatory or violative of the public interest, and that their preservation is consistent with the Energy Policy Act, most notably amended section 211 of the FPA. PacifiCorp and AEP express concern that contract abrogation

---

[158]*E.g.*, Dayton P&L, NSP, Montaup, Southwestern, Ohio Edison, Consumers Power, Allegheny, Public Generating Pool, NEPCO, Pennsylvania P&L, Southwest TDU Group, Arizona, DOD, El Paso, Florida Power Corp, AEC & SMEPA, Atlantic City, Texaco, Tampa, CSW, Central Illinois Public Service, CA Cogen, ConEd, GA Com, Consolidated Natural Gas, Ohio Valley, Pacific Northwest Coop, Salt River, Oglethorpe, Minnesota P&L, NYSEG, Brazos, Southern, Washington Water Power, CINergy, SoCal Edison, Hoosier EC.

[159]*E.g.*, AEC & SMEPA, Cajun, Carolina P&L, NSP, Pennsylvania P&L, UNITIL, Southwestern, CSW.

[160]*See also* Dairyland, DE Muni, Arkansas Cities, Ohio Valley.

would create competitive instability. American Forest & Paper argues that the Commission cannot refuse to honor existing contracts if it expects a competitive bulk power market to emerge.

Numerous commenters further argue that contract abrogation requires a fact-based, contract-specific evaluation, and they oppose any generic declaration that existing contracts are contrary to the public interest.[161] Some suggest that generic contract abrogation cannot be justified under the public interest standard.[162]

Missouri Basin MPA argues that the Commission should allow abrogation of existing wholesale power and transmission arrangements if the customer can demonstrate the undue competitive disadvantage caused by the arrangement.

---

[161]*E.g.*, AEP, Associated EC, DOD, El Paso, NEPCO, Ohio Edison, PSNM, Southwest TDU Group, Utilities For Improved Transition, NYSEG, Citizens Utilities, NM Com, EGA. See also NRECA, TDU Systems, Blue Ridge, CCEM, Industrial Energy Applications, APPA, Cajun, Springfield, DE Muni, Missouri Basin MPA, TANC, Wolverine Coop Members, FL Com, Citizens Utilities, Soyland (support contract abrogation on a case- by-case basis).

[162]*E.g.*, Utilities For Improved Transition, NSP, Southwestern, DE Muni.

A few commenters support some form of generic contract abrogation.[163] CCEM asserts that existing wholesale requirements customers must be given the right to convert to transmission service under non-discriminatory open access tariffs.[164] CCEM notes that this is the same relief from undue discrimination that the Commission afforded to pipeline customers in Order Nos. 436 and 500.[165] CCEM emphasizes that here, in contrast to what occurred in the gas industry, "[c]onversion rights should be understood as the logical quid pro quo for introducing extra-contractual stranded-cost recovery rights into the wholesale requirements **[31,663]** contracts of electric utilities."[166] NRECA asserts that it would be unduly discriminatory to allow new transmission customers to use the open access transmission tariffs, but not allow existing customers the same access.[167]

TAPS says that if those who now have discriminatory contracts are forced to live with those contracts, a fully

---

[163]*E.g.*, NRECA, CCEM, ELCON, DE Muni, Oglethorpe. Portland maintains that it would be in the public interest to abrogate existing contracts completely, but recommends that such action be taken only on a case-by-case basis.

[164]*See also* VT DPS, NYMEX.

[165]*See also* VT DPS, Portland.

[166]CCEM Initial Comments at p. 26. *See also* ELCON, VT DPS, Blue Ridge, NYMEX, OK Com, Missouri Basin MPA, Texas-New Mexico, TDU Systems.

[167]*See also* TDU Systems, Texas-New Mexico, TAPS, Wisconsin Municipals.

competitive market will be delayed considerably.[168] Moreover, TAPS argues, the Commission has a statutory duty to remedy the undue discrimination that it is only now recognizing. Even if the Commission will not abrogate these contracts across the board, TAPS asserts that we should use our section 206 authority to do so on a contract-by-contract basis.

San Francisco requests that the Commission clarify that a holder of capacity rights under an existing contract can extend contractual rights to transmission access at least coterminous with the life of the project and under a roll-over or renewal contract on the same basis as provided in the existing contract. Anoka EC proposes that when a wholesale purchaser's contract expires, it should have a right of first refusal to contract for the transmission capacity to which it previously had a right. Knoxville urges the Commission to require renegotiation of the notice and/or term of all existing contracts for which the voluntary termination period exceeds the time frame for implementation of the final rule.

NEPCO suggests that we require existing power contracts that allow rate changes to be separated into their generation and transmission components, without otherwise disturbing their terms; this would allow comparisons between

---

[168]*See also* NorAm. UtiliCorp argues that existing contracts should not be allowed to extend indefinitely (as through "evergreen" clauses) without adopting comparability. *See also* Texaco, Wisconsin Municipals, Phelps Dodge.

the transmission service the utility provides to its power customers and the service it offers to others.[169]

Coordination Agreements

CINergy argues that coordination agreements should not be excluded from the comparability standard and that the Commission should use its authority under section 206 to require amendments to such agreements, just as it did in Order 636 in requiring unbundling of pipeline supply contracts. CINergy suggests that public utilities should be given up to three years to file the amendments to avoid hardship on the industry and the Commission's staff. CINergy further asserts that future transactions conducted under coordination agreements should be unbundled and the transmission component subjected to the comparable transmission service requirement.

Others argue that purchases under existing coordination agreements made on behalf of retail native load should not be unbundled.[170] NY Com and IL Com recommend that proposed §35.28(c) be modified to state that the functional unbundling requirement "exclude(s) those wholesale purchases made by the utility to serve existing or expected native retail load."

Utilities For Improved Transition disagrees with the idea that new transactions under existing coordination

---

[169]*See also* Industrial Energy Applications.

[170]*E.g.*, Con Ed, Detroit Edison, IL Com.

agreements should be subject to the rule.[171] It argues that the sanctity of coordination contracts should be the same as for other contracts. Coordination contracts are not simply agreements to agree in the future, according to Utilities For Improved Transition; they set forth terms and rates and merely leave the timing of transactions to be resolved in the future. Moreover, it argues that the Commission has given no reason to abandon its practice of encouraging coordination sales by allowing price flexibility.

Commission Conclusion

Requirements and Transmission Contracts

We do not believe it is appropriate to order generic abrogation of existing requirements and transmission contracts. While the Commission did generically **[31,664]** find it appropriate to modify natural gas contracts to complete the move to a competitive commodity market in natural gas, we face a different situation here. At the time the Commission addressed this situation in the natural gas industry, it was faced with shrinking natural gas markets, statutory escalations in natural gas ceiling prices under the Natural Gas Policy Act, and increased production of gas.[172] In other words, there was a market failure in the industry that required the extraordinary measure of generically allowing all customers to break their contracts with pipelines.

---

[171]*See also* Utility Workers Union, VEPCO.

[172]*See* Pierce, Richard J., *Reconstituting the Natural Gas Industry from Wellhead to Burnertip*, 9 Energy L.J. 1 (1988).

In contrast, there is no such market failure in the electric industry. Although changes in the industry have been and continue to be dramatic, we do not believe they compel generic abrogation of requirements and transmission contracts.[173]

While we have concluded that current conditions in the wholesale power market do not warrant the generic modification of requirements contracts, we conclude nonetheless that the modification of certain requirements contracts on a case-by-case basis may be appropriate. We conclude further that, even if customers under such contracts are bound by so-called Mobile-Sierra clauses, they nonetheless ought to have the opportunity to demonstrate that their contracts no longer are just and reasonable.

The Commission finds that it would be against the public interest to permit a Mobile-Sierra clause in an existing wholesale requirements contract to preclude the parties to such a contract from the opportunity to realize the benefits of the competitive wholesale power markets. For purposes of this finding, the Commission defines existing requirements contracts as contracts executed on or before July 11, 1994.[174]

---

[173]In addition, we do not believe that unfavorable requirements contracts will derail the attainment of competitive wholesale power markets. Indeed, many of the commenters support this position and seek to retain their existing requirements contracts.

[174]This is consistent with the definition of existing requirements contracts we have used for purposes of stranded cost recovery.

By operation of this finding, a party to a requirements contract containing a Mobile-Sierra clause no longer will have the burden of establishing independently that it is in the public interest to permit the modification of such contract. The party, however, still will have the burden of establishing that such contract no longer is just and reasonable and therefore ought to be modified.

This finding complements the Commission's finding that, notwithstanding a Mobile-Sierra clause in an existing requirements contract, it is in the public interest to permit amendments to add stranded cost provisions to such contracts if the public utility proposing the amendment can meet the evidentiary requirements of this Rule.[175] The Commission's complementary Mobile-Sierra findings are not mutually exclusive. Any contract modification approved under this Section shall provide for the utility's recovery of any costs stranded consistent with the contract modification. The stranded costs must be prudently incurred, legitimate and verifiable, as provided in Section IV.J. Further, the Commission has concluded that if a customer is permitted to argue for modification of existing contracts that are less favorable to it than other generation alternatives, then the utility should be able to seek modification of contracts that may be beneficial to the customer.

The Commission believes that the most productive way to analyze contract modification issues is to consider simultaneously both the selling public utility's claims, if any, that it had a reasonable expectation of continuing to serve the

---

[175]*See* Section IV.J.5.

customer beyond the term of the contract and the customer's claim, if any, that the contract no longer is just and reasonable and therefore ought to be modified. Thus, if the selling public utility intends to claim stranded costs, it must present that claim in any section 206 proceeding brought by the customer to shorten or terminate the contract. Similarly, if the customer intends to claim that the notice or termination provision of its existing requirements contract is unjust and unreasonable, it must present that claim in any proceeding brought by the selling public utility to seek recovery of stranded costs. This will promote administrative **[31,665]** efficiency and will permit the Commission to consider how the contracting parties' claims bear on one another.

The Commission does not take contract modification lightly. Whether a utility is seeking a contract amendment to permit stranded cost recovery based on expectations beyond the stated term of the contract, or a customer is seeking to shorten or eliminate the term of an existing contract, we believe that each has a heavy burden in demonstrating that the contract ought to be modified. Still, we believe that given the industry circumstances now facing us, both selling utilities and their customers ought to have an opportunity to make the case that their existing requirements contracts ought to be modified. By providing both buyers and sellers this opportunity, the Commission attempts to strike a reasonable balance of the interests of all market participants. The Commission expects that many of the arguments presented by buyers and sellers in such proceedings will be fact specific.

We note that because we are not abrogating existing requirements and transmission contracts generically and because the functional unbundling requirement of the Final

Rule applies only to new wholesale services, the terms and conditions of the Final Rule pro forma tariff do not apply to service under existing requirements contracts. However, if a customer's existing bundled service (transmission and generation) contract or transmission-only contract expires, and the customer takes any new transmission service from its former supplier, the terms and conditions of the Final Rule tariff would then apply to the transmission service that the customer receives.

A further issue concerning firm contract customers is their right to transmission capacity (and the rate for such capacity) when their contracts expire by their own terms or become subject to renewal or rollover. We have concluded that all firm transmission customers (requirements and transmission-only), upon the expiration of their contracts or at the time their contracts become subject to renewal or rollover, should have the right to continue to take transmission service from their existing transmission provider. The limitations are that the underlying contract must have been for a term of one-year or more and the existing customer must agree to match the rate offered by another potential customer, up to the transmission provider's maximum filed transmission rate at that time, and to accept a contract term at least as long as that offered by the potential customer.[176] This means that there is no right to grandfather

---

[176]This right of first refusal exists whether or not the customer buys power from the historical utility supplier or another power supplier. If the customer chooses a new power supplier and this substantially changes the location or direction of its power flows, the customer's right to continue taking transmission service from its existing transmission provider may be affected by

the historical price of the transmission service. Thus, if not enough capacity is available to meet all requests for service, the right of first refusal gives the capacity to the existing customer who had contractually been using the capacity on a long-term, firm basis, assuming that it meets the conditions set forth above. Moreover, this limited right of first refusal is not a one-time right of first refusal for contracts existing as of the date of the final rule, but is an ongoing right that may be exercised at the end of all firm contract (including all future unbundled transmission contracts) terms. A customer converting existing bundled service to the Final Rule pro forma tariff would not have a reservation priority for capacity expansions, unless the existing contract provides for future transmission to the customer that requires capacity expansion.[177]

Finally, with respect to all existing requirements contracts and tariffs that provide for bundled rates, we will require all public utilities to make informational filings setting forth the unbundled power and transmission rates reflected in those contracts and tariffs. These informational rates must be submitted to the Commission within 60 days of publication of the Final Rule in the Federal Register and must also be included as a line item on all bills submitted to wholesale customers in the third month following the effective date of this final rule. The unbundled **[31,666]** informational rates will permit wholesale customers to compare rates in

---

transmission constraints associated with the change.

[177]The above discussion on a right of first refusal addresses firm contract customers. However, the same logic applies to retail customers.

anticipation of their contracts expiring so that they can evaluate alternative contracts. Coordination Agreements

The situation as to coordination agreements requires a slightly different approach.[178] While we also believe that as a general matter it is important not to generically abrogate any coordination agreements, this is particularly true for non-economy energy coordination agreements that may reflect complementary long-term obligations among the parties. This type of agreement presents special problems and, as discussed below, we will not generically require this type of coordination agreement to be modified.[179]

Hundreds of coordination agreements exist in the industry today. Many are open-ended agreements that permit new transactions to occur well into the future. Because these contracts may not expire of their own terms in a reasonable

---

[178]For purposes of this discussion, we define coordination agreements as all power sales agreements, except requirements service agreements. In addition, for purposes of implementing the non-discriminatory, open access requirements of the Final Rule, we are dividing bilateral coordination agreements into two general categories: (1) *Economy energy coordination agreements* are contracts and service schedules thereunder that provide for trading of electric energy on an "if, as, and when available" basis, but do not require either the seller or buyer to engage in a particular transaction; and (2) *non-economy energy coordination agreements* are any non-requirements service agreements, except economy energy coordination agreements.

[179]The requirements for power pools and other multilateral arrangements are discussed in detail in Section IV.F.

time, they may present a larger and more enduring obstacle to non-discriminatory open access and more competitive bulk power markets. Thus, to assure that non-discriminatory open access becomes a reality in the relatively near future, we will partially modify existing economy energy coordination agreements. We will condition future sales and purchase transactions under existing economy energy coordination agreements[180] to require that the transmission service associated with those transactions be provided pursuant to this Rule's requirements of non-discriminatory open access, no later than December 31, 1996.[181] We also will require that for new economy energy coordination agreements[182] where the transmission owner uses its transmission system to make economy energy sales or purchases, the transmission owner must take such service under its own transmission tariff as of the date trading begins under the agreement.[183]

---

[180]Those executed prior to 60 days after publication of the Open Access Rule in the *Federal Register*.

[181]The requirement to unbundle future transactions under existing economy energy coordination agreements means that if the transmission owner uses its transmission system to make economy energy coordination sales or purchases, it must take service for these transactions under its own transmission tariff after December 31, 1996.

[182]Those executed 60 days after publication of the Open Access Rule in the *Federal Register*.

[183]Accordingly, transmission service needed for sales or purchases under *all* new economy energy coordination agreements will be pursuant to the Final Rule pro forma tariff.

Finally, we will treat non-economy energy coordination agreements differently. We will not require their modification. However, this does not insulate such agreements from complaints that transmission service provided under such agreements be provided pursuant to the Final Rule pro forma tariff.

With respect to coordination pricing practices, we conclude that non-discriminatory open access consistent with the requirements of this Rule is necessary if we are to allow utilities to continue to use market-driven pricing, such as split-the-savings pricing, for coordination sales. Absent such non-discriminatory open access, a utility would be able to deny access to others so as to obtain a higher price for its own power sales.

6. Flow-Based Contracting and Pricing

In the NOPR, the Commission discussed the procedures to be used in establishing Stage One rates. These Stage One rates were proposed as an administrative convenience. The proposal merely followed the long-established practice of establishing rates on the basis of contract **[31,667]** path pricing.[184] The Commission made no

---

[184]A contract path is simply a path that can be designated to form a single continuous electrical path between the parties to an agreement. Because of the laws of physics, it is unlikely that the actual power flow will follow that contract path.

determination with respect to the appropriateness of flow-based pricing or contracting for other purposes.[185]

Most of the commenters addressing this issue recommend that industry or the Commission -- either in this rule or ultimately -- dispense with the traditional contract path basis for pricing and contracting. Most commenters also recommend that the Commission adopt or encourage a regional approach to the solution of transmission pricing problems, though they differ markedly in how to account for flows.[186]

Transmission customers generally seek to rid themselves of "pancaked" transmission rates that are associated with the traditional approach to transmission pricing.[187] They propose the development of regionwide transmission rates, perhaps determined on a pool or RTG

---

[185]Flow-based pricing or contracting would be designed to account for the actual power flows on a transmission system. It would take into account the "unscheduled flows" that occur under a contract path regime.

[186]*E.g.*, APPA, TAPS, NY Energy Buyers, Arcadia, Brownsville, Detroit Edison Customers, AMP-Ohio, Michigan Systems.

[187]*E.g.*, AMP-Ohio, NRECA, APPA, Detroit Edison Wholesale Customers, MMWEC, Missouri Basin MPA, Air Liquide, American Wind Energy, Associated Power, CCEM.

basis. Most, however, do not discuss how to account for unscheduled flows.[188]

Many transmission providers, some regulatory authorities, and some individuals strongly support flow-based pricing. Most of these commenters recognize a need for a regional approach to resolve transmission pricing concerns.[189] However, many of them also appear to accept contract pricing in the near term because of the need to implement open access quickly. [190]NERC recommends that the Commission maintain an open position on the transfer scheduling process and supports changes in the process to reflect actual power flows. EEI suggests that the Commission should be willing to deviate from a contract path approach, since competition may be accompanied by greater unscheduled flows and contract pricing is not well equipped to deal with such flows.

---

[188]Some commenters propose the development of a regional rate on a postage stamp basis, without regard to distance travelled or the actual path of power flows. *E.g.*, Air Liquide, American National Power, CA Energy Co. Several commenters do, however, propose ways to account for unscheduled flows. *E.g.*, American Forest & Paper, DE Muni, Lower Colorado River Authority.

[189]*E.g.*, CSW, EDS Utilities, Dominion, CINergy, KS Com, CT DPUC, Com Ed, Hogan.

[190]NYMEX favors contract path pricing because of its familiarity and believes that the issue should primarily be resolved by the transmitting utilities. AEP believes that the primary responsibility lies with industry to develop alternative pricing structures.

However, EEI concludes that a single approach to pricing will not be appropriate for all systems.

Other commenters, however, do raise concerns with respect to flow-based pricing. AEC & SMEPA considers flow-based pricing to be flawed because that method makes an individual customer responsible for load flow effects caused by a third party's development of the third-party's transmission system over which the customer and its transmission provider had no control. Dayton P&L fears that competition would be lessened under flow- based pricing because utilities with large transmission systems would dominate the market.

Several commenters oppose Southern's and United Illuminating's flow-based proposals, arguing that the methodologies are based on estimates of actual flows or a set of conditions with limited applicability. Various commenters also believe that a single rate is flawed and could cause just as many problems as contract path pricing.[191]

Most commenters appear to believe that the Commission endorsed contract path pricing in the NOPR. Hogan expresses concern that many industry participants' understanding of the pro forma tariffs is based on the fiction of the contract path. The MT Dept of Environmental **[31,668]** Quality believes that despite the Commission's pledge to consider innovative pricing proposals,[192] such proposals will

---

[191] *E.g.*, NU, NEPCO, BECO, Florida Power Corp.

[192] *See FERC Statutes and Regulations* ¶31,005.

receive heavy scrutiny, while conventional contract path pricing proposals will receive nearly automatic approval. Dominion is concerned that relying on the initiative of individual transmission owners to develop flow- based pricing will yield slow and patchy results.

Commission Conclusion

We will not, at this time, require that flow-based pricing and contracting be used in the electric industry. In reaching this conclusion, we recognize that there may be difficulties in using a traditional contract path approach in a non- discriminatory open access transmission environment, as described by Hogan and others. At the same time, however, contract path pricing and contracting is the longstanding approach used in the electric industry and it is the approach familiar to all participants in the industry. To require now a dramatic overhaul of the traditional approach -- such as a shift to some form of flow-based pricing and contracting -- could severely slow, if not derail for some time, the move to open access and more competitive wholesale bulk power markets. In addition, we believe it is premature for the Commission to impose generically a new pricing regime without the benefit of any experience with such pricing. We welcome new and innovative proposals, but we will not impose them in this Rule.

While we are not requiring the use of any form of flow-based pricing, we recognize that some versions of flow-based pricing could have benefits. For example, some versions of flow-based pricing could more accurately reflect and price the actual power flows on transmission systems and thus could produce efficiency gains, better generation siting

decisions, and benefits for customers and utilities alike. Other versions could more accurately assign capacity rights in accordance with a party's contribution to capacity costs.

These potential benefits, however, will not simply come about in the abstract. Flow-based pricing methodologies that will achieve the benefits sought by most of the participants in the industry are in a development stage and require further work and refinement to address some of the difficulties associated with flow-based approaches. Concurrent work on OASIS and resolving available transmission capability issues may help resolve flow-based issues. However, as demonstrated by the paucity of possible methodologies presented in the comments, developing workable methodologies will be difficult. As we explained in our Transmission Pricing Policy Statement, we are receptive to proposals for alternative rate methodologies, such as distance-sensitive and flow-based pricing, as long as the proposals are well supported. However, we have yet to receive a formal rate application for a flow-based pricing methodology that has been tested enough that it can be required on a generic basis. Thus, we have decided to go forward to achieve open access and more competitive wholesale bulk power markets without waiting for the development of a generic flow-based pricing methodology.

We wish to emphasize further that in taking this approach we are not endorsing the traditional contract path approach as the only available approach. We continue to approve contract path pricing because it is the long-established pricing method that comes to us in rate filings by the electric industry, is administratively convenient and feasible, and thus is a practical way to move forward now. We remain open to

alternative methodologies, but need to see better developed approaches from the industry before we can consider generic adoption of alternative pricing.

We also believe the adoption of flow-based pricing will be more practical on a regional, instead of individual utility, basis. Some forms of flow-based pricing may even require a regional approach. To this extent, regional ISOs could be a valuable mechanism for implementing such pricing reforms.

B. *Legal Authority*

The Commission reaffirms its conclusion in the NOPR that we have the authority under the FPA to order wholesale transmission services in interstate commerce to remedy undue discrimination by public utilities. We analyze below the relevant cases examining our wheeling authority, **[31,669]** then discuss and respond to the legal arguments raised by the commenters.

1. Bases for Legal Authority

a. Undue Discrimination/Anticompetitive Effects

In upholding the Commission's order requiring non-discriminatory open access in the natural gas industry, the court in Associated Gas Distributors v. FERC stated that the Natural Gas Act "fairly bristles" with concern for undue

discrimination.[193] The same is true of the FPA. The Commission has a mandate under sections 205 and 206 of the FPA to ensure that, with respect to any transmission in interstate commerce or any sale of electric energy for resale in interstate commerce by a public utility, no person is subject to any undue prejudice or disadvantage. We must determine whether any rule, regulation, practice or contract affecting rates for such transmission or sale for resale is unduly discriminatory or preferential, and must prevent those contracts and practices that do not meet this standard. As discussed below, AGD demonstrates that our remedial power is very broad and includes the ability to order industry- wide non-discriminatory open access[194] as a remedy for undue discrimination. The AGD court reached this decision even in the face of prior cases that acknowledged that Congress did not mandate common carriage or explicitly empower the Commission to order direct access for either gas transporters or electric utilities. Moreover, the Commission's power under the FPA "clearly carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of interstate utility operations pursuant to

---

[193]*Associated Gas Distributors v. FERC*, 824 F.2d 981, 998 (D.C.Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988) (AGD).

[194]We use the term "open access" to refer to a public utility's obligation to put a tariff on file offering service to eligible customers. Access is not open to all. Specifically, the tariff is not an offer to serve retail customers if state law does not permit retail wheeling.

(FPA) sections 202 and 203, and under like directives contained in sections 205, 206, and 207."[195]

Therefore, based on the mandates of sections 205 and 206 of the FPA and the case law interpreting the Commission's authority over transmission in interstate commerce, we conclude that we have ample legal authority -- indeed, a responsibility -- under section 206 of the FPA to order the filing of non-discriminatory open access transmission tariffs if we find such order necessary as a remedy for undue discrimination or anticompetitive effects.[196] We discuss below the primary court decisions that touch on our wheeling authority under sections 205 and 206.

The Commission's authority to order access as a remedy for undue discrimination under the Natural Gas Act (NGA) was upheld and discussed in detail in AGD. In AGD, the court upheld in relevant part the Commission's Order No.

---

[195]*Gulf States Utilities Company v. FPC*, 411 U.S. 747, 758-59 (1973).

[196]In most situations, discrimination that precludes transmission access or gives inferior access will have at least potential anticompetitive effects because it limits access to generation markets and thereby limits competition in generation. Similarly, it is probable that any transmission provision that has anticompetitive effects would also be found to be unduly discriminatory or preferential because the anticompetitive provision would most likely favor the transmission owner vis-a-vis others.

436.[197] That order found the prevailing natural gas company practices to be "unduly discriminatory" within the meaning of section 5 of the NGA (the parallel to section 206 of the FPA) and held that if pipelines wanted blanket certification for their transportation services, they must commit to transport gas for others on a non-discriminatory basis; in other words, they must provide non-discriminatory open access.

In upholding the Commission's authority to require open access, the court first noted that the opponents' arguments against such authority must proceed "uphill." The statute contains no language forbidding the Commission to impose common carrier status on pipelines, let alone forbidding the Commission to impose "a specific duty that happens to be a typical or even core component of such status." The court found that the legislative **[31,670]** history cited by the opponents came nowhere near overcoming this statutory silence. Rather, the legislative history supported only the proposition that Congress itself declined to impose common carrier status.[198] Emphasizing Congress' deep concern with undue discrimination, the court found that the Commission had ample authority to "stamp out" such discrimination:

The issue seems to come down to this: Although Congress explicitly gave the Commission the power and the duty to achieve one of the prime goals of common carriage

---

[197]Order No. 436, Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, *FERC Statutes and Regulations* ¶30,665 (1985).

[198]*AGD*, *supra*, 824 F.2d at p. 997.

regulation (the eradication of undue discrimination), the Commission's attempted exercise of that power is invalid because Congress in 1906 and 1914 and 1935 and 1938 itself refrained from affixing common carrier status directly onto the pipelines and from authorizing the Commission to do so. And this proposition is said to control no matter how sound the Order may be as a response to the facts before the Commission. We think this turns statutory construction upside down, letting the failure to grant a general power prevail over the affirmative grant of a specific one.[199]

The AGD court found that court decisions under the FPA did not support the view that the Commission's authority to "stamp out" undue discrimination is hamstrung by an inability to require non-discriminatory open access as a remedy. These decisions are discussed below.

One of the earliest cases on wheeling is Otter Tail Power Company v. United States (Otter Tail).[200] In that case, the Supreme Court rejected the argument that the District Court, in a civil antitrust suit, could not order wheeling because to do so would conflict with the FPC's purported wheeling authority.[201] The Court explained that Congress had decided not to impose a common carrier obligation on the electric power industry and noted that the Commission was

---

[199]*Id.* at p. 998.

[200]410 U.S. 366 (1974).

[201]410 U.S. at pp. 375-76.

not at that time expressly granted power to order wheeling.[202] In effect, it concluded that because Congress did not include common carrier provisions in the FPA, the Commission must not have any express authority to order wheeling that would preclude the District Court from imposing a wheeling remedy. Nowhere, however, did the Court say that the Commission lacked authority under section 206 to remedy undue discrimination. Indeed, that was simply not a matter before the Court or of any consequence to its decision.

In the FPA, while Congress elected not to impose common carrier status on the electric power industry, it tempered that determination by explicitly providing the Commission with the authority to eradicate undue discrimination -- one of the goals of common carriage regulation.[203] By providing this broad authority to the Commission, it assured itself that in preserving "the voluntary action of the utilities" it was not allowing this voluntary action to be unfettered. It would be far-reaching indeed to conclude that Otter Tail, which was a civil antitrust suit that raised issues entirely unrelated to our authority under section 206, is an impediment to our achieving one of the primary goals of the FPA -- eradicating undue discrimination in transmission in interstate commerce in the electric power industry.

In Richmond Power & Light Company v. FERC (Richmond),[204] the FPC, in reaction to the 1973 oil embargo,

---

[202] *Id.* at pp. 374-76.

[203] *See AGD*, 824 F.2d at p. 998.

[204] 574 F.2d 610 (D.C. Cir. 1978).

was attempting to reduce dependence on oil. The FPC requested that utilities with excess capacity wheel power to the New England Power Pool (NEPOOL). In response, several suppliers and transmission owners filed rate schedules. with the FPC that provided for voluntary wheeling. Richmond Power & Light Company (Richmond) objected to these filings, claiming that they were unreasonable because they did not guarantee transmission access. The FPC refused to compel the utilities to wheel Richmond's power, stating that it did not have the authority to order a public utility to act as a common carrier.

The D.C. Circuit upheld the Commission. It acknowledged that Richmond's argument was persuasive in some respects, **[31,671]** but stated that any conditions the Commission might impose could not contravene the FPA. The court examined the legislative history of the FPA and stated that "[i]f Congress had intended that utilities could inadvertently bootstrap themselves into common- carrier status by filing rates for voluntary service, it would not have bothered to reject mandatory wheeling * * *."[205]

However, the D.C. Circuit in no way indicated that the Commission was foreclosed from ordering transmission as a remedy for undue discrimination. Richmond also had argued that the alleged refusal of the American Electric Power Company (AEP) and its affiliate, Indiana & Michigan Electric Company (Indiana), to wheel Richmond's excess energy was unlawful discrimination because AEP and Indiana wheeled higher-priced electricity from other AEP affiliates. The court

---

[205] *Id.* at p. 620.

acknowledged that Richmond's claim of unlawful discrimination was theoretically valid, but found that Richmond had failed to prove its case. It noted that if Richmond had argued that the rates were unjustifiably discriminatory, or that Indiana's failure to use its transmission capability fully or to purchase less expensive electricity for wheeling resulted in unnecessarily high rates, a different case would be before the court.[206] The case thus does not in any way limit the Commission's authority to remedy undue discrimination.

In Central Iowa Power Cooperative v. FERC,[207] the FPC[208] reviewed the terms of the Mid-Continent Area Power Pool (MAPP) Agreement under its section 205 and 206 authority. The agreement contained two membership limitations. First, the agreement established two classes of membership, with one class being entitled to more privileges than the other. Second, the agreement excluded non-generating distribution systems from pool services. The FPC found the first limitation on membership -- the two-class system -- to be unduly discriminatory and not reasonably related to MAPP's objectives. The FPC conditioned approval of the agreement under section 206 on the removal of the unduly discriminatory provision. The FPC found that the

---

[206] *Id.* at p. 623, nn.53 and 57.

[207] 606 F.2d 1156 (D.C. Cir. 1979).

[208] While *Central Iowa* was pending, certain of the functions of the FPC were transferred to the FERC under the DOE Organization Act. Accordingly, the FERC was substituted for the FPC as the respondent in the case.

second limitation, the exclusion of non-generating distribution systems, was not anticompetitive and did not render the agreement inconsistent with the public interest.

On appeal, the D.C. Circuit affirmed the FPC's decision. The court found that the FPC did have authority to order changes in the scope of the MAPP agreement, if the agreement was unjust, unreasonable, unduly discriminatory or preferential under section 206 of the FPA. The court stated:

> The Commission had authority, * * * under section 206 of the Act, * * * to order changes in the limited scope of the Agreement, including the addition of pool services, if, in the absence of such modifications, the Agreement presented "any rule, regulation, practice or contract (that was) unjust, unreasonable, unduly discriminatory or preferential."[209]

However, the court agreed with the FPC's conclusion that the limited scope of MAPP was not unjust, unreasonable, or unduly discriminatory. The court recognized that a pool was not invalid under section 206 merely because a more comprehensive arrangement was possible.

The D.C. Circuit upheld the Commission's refusal to eliminate the second limitation on membership by ordering MAPP participants to wheel to non-generating electric systems.[210] However, neither the Commission nor the court was presented with the argument that wheeling was necessary as a remedy for undue discrimination.

---

[209] 606 F.2d at p. 1168.

[210] *Id.* at p. 1169; *see also Municipalities of Groton v. FERC*, 587 F.2d 1296 (D.C. Cir. 1978).

In Florida Power & Light Company v. FERC (Florida),[211] the Commission ordered Florida Power & Light Company (FP&L) to file a tariff setting forth FP&L's policy relating to the availability **[31,672]** of transmission service.[212] FP&L objected to including such a policy statement in its tariff and argued that the filing of such a policy would convert FP&L into a common carrier by obligating it to offer service to all customers.[213] There was no finding that the action ordered was necessary to remedy undue discrimination.

The Fifth Circuit Court of Appeals agreed with FP&L that the mandatory filing of the policy statement would require FP&L to provide transmission service beyond its voluntary commitment because such a requirement would

---

[211]660 F.2d 668 (5th Cir. 1981), *cert. denied sub nom. Fort Pierce Utilities Authority v. FERC*, 459 U.S. 1156 (1983).

[212]FP&L provided transmission service when four conditions were met: (1) the specific potential seller and buyer were contractually identified; (2) the magnitude, time and duration of the transaction were specified prior to the commencement of the transmission; (3) it could be determined that the transmission capacity would be available for the term of the contract; and (4) the rate was sufficient to cover FP&L's costs.

[213]All utilities requesting wheeling services, subject to availability, would be entitled to receive transmission service under the filed terms. Any changes to a filed rate must be filed with the Commission. This is the so-called "filed rate doctrine." *See Northwestern Public Service Company v. Montana-Dakota Utilities Company*, 181 F.2d 19, 22 (8th Cir. 1980), aff'd, 341 U.S. 246 (1951).

change its duties and liabilities.[214] The Commission order would impose common carrier status on FP&L, the court found.[215] The court noted that the Commission did not rely on a finding of anticompetitive behavior and therefore the court did not address the Commission's power to remedy antitrust violations.[216]

The AGD court explicitly rejected the claim that the above line of cases establishes that the Commission lacks authority to require non-discriminatory open access.[217] Opponents of the Commission's order argued in AGD that Richmond and Florida, supra, stand for the proposition that the Commission cannot indirectly do what it allegedly cannot do directly, that is, impose common carriage. The AGD court

---

[214]Under the filed rate doctrine, a refusal to wheel would be unduly discriminatory under section 206 of the FPA. As the court acknowledged, a customer refused service could petition the Commission to find that FP&L's policy of availability was unduly discriminatory under section 206(a) of the FPA. The court said that in the absence of a tariff on file, a utility refused wheeling services would be unable to claim discrimination under section 206(a) of the FPA. 660 F.2d at p. 675 (expressing "serious doubts that such a petition would be successful in the absence of a tariff").

[215]*Id.* at p. 676.

[216]*Id.* at p. 678.

[217]The AGD court did not address *New York State Electric & Gas Corporation v. FERC*, 638 F.2d 388 (2d Cir. 1980), cert. denied, 454 U.S. 821 (1981) (NYSEG), presumably because that case did not concern whether the Commission could order wheeling as a remedy for undue discrimination.

rejected these arguments, stating that the petitioners read the electric cases far too broadly:

(n)either Richmond nor Florida comes anywhere near stating that the Commission is barred from imposing an open-access condition in all circumstances.[218]

The court noted that the Florida case had expressly left open the question of whether the Commission would be entitled to use an open access condition as a remedy for anticompetitive conduct, and that in Richmond the D.C. Circuit had said little more than that unwillingness to transmit for all could not be automatically deemed undue discrimination. The court also noted the Central Iowa case, supra, in which it had upheld a Commission order that found a power pooling agreement discriminatory on its face because the agreement gave one class of membership privileged status over another. The court stated that the Central Iowa case "upholds the power of the Commission to subject approval of a set of voluntary transactions to a condition that providers open up the class of permissible users."[219] The court added that it refused to "turn statutory construction upside down" by letting Congress' failure to grant a general power of common carriage prevail over the affirmative grant of the specific power to eradicate undue discrimination.[220]

---

[218]824 F.2d at p. 999

[219]*Id.* at p. 999.

[220]*Id.* at p. 1006.

We conclude that AGD's analysis of undue discrimination under sections 4 and 5 of the Natural Gas Act is equally applicable to an undue discrimination analysis under sections 205 and 206 of the **[31,673]** FPA. The Commission and courts have long recognized that the NGA was patterned after the FPA and that the two statutes should be interpreted in the same manner.[221] Thus, we conclude that we have the authority to remedy undue discrimination and anticompetitive effects by requiring all public utilities that own, control or operate transmission facilities to file non-discriminatory open access transmission tariffs.

b. Section 211 of the Federal Power Act

In concluding that we must invoke our section 206 authority to remedy undue discrimination and anticompetitive effects in the electric industry, we have carefully considered the goals of Title VII of the Energy Policy Act, and whether section 211 of the FPA, by itself, is sufficient to remedy undue discrimination in public utility transmission services. Title VII of the Energy Policy Act, which amended section 211 of the FPA to give the Commission broader authority to order wheeling in the public interest on a case-by-case basis, reflects the intent of Congress to encourage competitive wholesale electric markets. Section 211 provides a means for

---

[221]*See, e.g., FPC v. Sierra Pacific Power Company*, 350 U.S. 348, 353 (1956); *Arkansas Louisiana Gas Company v. Hall*, 453 U.S. 571, 577 n.7 (1981); and *Kentucky Utilities Company v. FERC*, 760 F.2d 1321, 1325 n.6 (D.C. Cir. 1985). Section 206 of the FPA was recently revised and now differs from section 5 of the NGA, but not in a manner significant to our discussion here. See 16 U.S.C. 824e(b) and (c).

wholesale power sellers and buyers to obtain transmission services necessary to compete in, or to reach, competitive markets, and is a valuable tool to encourage competitive markets. However, in amending section 211, Congress left unaltered the authorities and obligations of the Commission under sections 205 and 206 (similar to our authorities and obligations under sections 4 and 5 of the NGA) to remedy undue discrimination. In addition, as discussed below, reliance on section 211 alone in some circumstances can result in the perpetuation of, rather than the elimination of, undue discrimination and anticompetitive effects.

First, there are inherent delays in the procedures for obtaining service under section 211. However, for competitive reasons, many transactions must be negotiated relatively quickly. Many competitive opportunities will be lost by the time the Commission can issue a final order under section 211. Case-by-case section 211 proceedings are not a substitute for tariffs of general applicability that permit timely, non-discriminatory access on request.

Second, discrimination is inherent in the current industry environment in which some customers and sellers are served by open access systems, and others have to rely on negotiated bilateral arrangements or the mandatory section 211 process. The end result is discrimination in the ability to obtain transmission services, as well as in the quality and prices of the services. This national patchwork of open and closed transmission systems, with disparate terms and conditions of service, cannot be cured effectively through section 211.

The Commission believes that its actions under sections 205 and 206 will complement the section 211 procedures to achieve both the Energy Policy Act's goals of creating more competitive bulk power markets and lower rates for consumers and the Federal Power Act's explicit direction in section 205(b) that no public utility shall, with respect to any transmission in interstate commerce, grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage.

2. Response to Commenters Opposing our Legal Authority

a. Authority to Order Open Access Tariffs

Initial Comments Supporting Commission Authority

A number of commenters support or state that they do not oppose the Commission's authority to order open access tariffs.[222] NIEP and CCEM explain that the AGD decision supports the Commission's action in this proceeding. ELCON asserts that the Commission's "extensive treatment of the relevant case law demonstrating FERC's authority to remedy this discrimination is legally sound." UtiliCorp argues that section 211 supports, rather than undermines, the Commission's **[31,674]** authority for the NOPR because it reflects Congress's intention to encourage more competitive bulk power markets.

---

[222]NIEP, ELCON, CINergy, UtiliCorp, TAPS, SBA, Entergy, NY Energy Buyers, Sierra.

Initial Comments Opposing Commission Authority

Other commenters assert that the Commission has improperly relied on sections 205 and 206 of the FPA to require open access.[223] They argue, for instance, that Otter Tail should be read as a broad constraint on the Commission's authority to order wheeling for any purpose and that the AGD decision does not undermine that holding or the cases following Otter Tail.[224] In support, some of these commenters discuss Richmond Power & Light, New York State Electric & Gas Corporation, and Florida Power & Light Company, the same cases discussed by the Commission in the NOPR.[225]

For example, EEI highlights the AGD court's discussion noting the difference between the legislative history of the NGA and that of the FPA, which the court stated was not as strong as that of the NGA. Moreover, EEI argues that the court found that section 7 of the NGA provided support for the Commission's actions in Order No. 436 and that such section 7 conditioning authority is lacking under the FPA. Allegheny notes that AGD did not overrule Otter Tail. Dayton P&L states that, in the gas case, the Commission was

---

[223]*E.g.*, EEI, Atlantic City, Allegheny, VA Com, PA Com, Ohio Edison, Southern, Utilities For Improved Transition, Dayton P&L, SCE&G, Centerior, BG&E, Central Hudson, NY Com, Salt River, Carolina P&L, Union Electric, VEPCO, Utility Workers Union.

[224]EEI, VA Com, Union Electric.

[225]E.g., EEI, VA Com, NY Com, PA Com, Salt River, Southern, Dayton P&L, Detroit Edison, BG&E.

responding to voluntary filings by pipelines. It also says that before the NOPR, the Commission itself saw its authority as more limited. SCE&G points to differences between Commission jurisdiction over public utilities and gas pipelines and criticizes the Commission's alleged assumption that the circumstances involved in the gas and electric industries are virtually identical.

PA Com argues that the attempt to analogize to the NGA and the cases that refer to that Act is inconsistent with the technical and engineering realities of the electric transmission grid and that extensive comparisons between the natural gas industry and the electric industry are misleading.[226]

FL Com argues that, in relying on sections 205 and 206 to establish generic open access transmission tariffs for all public utilities, the Commission violates the court's decision in Cajun Electric Power Cooperative v. FERC, 28 F.3d 173 at 179 (D.C. Cir. 1994), where, FL Com argues, the court refused to allow the Commission to use a non-evidentiary ruling when there were material facts at issue.

Reply Comments

CCEM responds that EEI and others confuse the obligations of a common carrier with the duty of public utilities not to unduly discriminate. It says that AGD supports the Commission's authority because the legislative history of

---

[226]See also NY Com (NGA has no parallel provision to section 211 of the FPA), Salt River.

the FPA and the NGA are similar with respect to common carriage. According to CCEM, early versions of both statutes would have made the regulated industries operate as common carriers (citing Otter Tail, the legislative history of the FPA, the legislative history of the Public Utility Holding Company Act, and the legislative history of the Mineral Leasing Act), but that Congress chose not to impose the common carrier obligations.

CCEM also says that the duties the Commission imposed on the gas industry and those in the NOPR are not common carriage in any event. According to CCEM, a common carrier must carry all goods offered (citing Am. Trucking Assoc. v. Atchison, T. & S.F. Ry. Co., 387 U.S. 397, 406 (1967)). Finally, CCEM cites Stephenson v. Binford, 287 U.S. 251, 265-66 (1932), where the Supreme Court held that obligations that are typical of common carriers can be imposed on contract motor carriers.

CCEM further disagrees with EEI's argument that the enactment of section 211 was a disavowal of any other Commission authority to order transmission.

[31,675]

ELCON also disagrees with EEI's claim that the Energy Policy Act undermines the Commission's pre-existing section 205 and 206 authority. It states that the savings clause in section 212(e) of the FPA, as amended, explicitly expresses Congress' intention not to undermine the Commission's pre-existing authority and that the legislative history contains nothing to suggest otherwise.

Similarly, in response to those who argue that section 211 is the only source of authority for the Commission to order transmission, NIEP argues that sections 211 and 212 serve purposes different from section 206. It says that the Commission's authority to order transmission in the "public interest" under sections 211 and 212 is not synonymous with its authority to order transmission as a remedy for undue discrimination under section 206; the two standards are complementary but distinct:

Although broadly applicable, the Commission's ability to order wheeling under Sections 211 and 212 is carefully limited by a number of procedural provisions. Foremost among these is the requirement that the wheeling may be ordered only upon a specific application for transmission services. FERC's authority to act in the public interest is thus confined to the individual case.

By contrast, FERC's remedial powers under Section 206 can be exercised upon a finding of unjust, unreasonable or unduly discriminatory or preferential practices. Once that finding has been made, however, the form and substance of the remedy is left entirely to the FERC's discretion. If FERC deems it necessary, FERC may adopt generally applicable rules or practices as a countermeasure to discriminatory acts, including ordering utilities to file generally applicable transmission tariffs.[227]

NIEP also points out that the legislative history does not address the Commission's authority to order transmission

---

[227]NIEP Reply Comments at p. 8.

as a remedy for undue discrimination. It challenges the interpretation of the legislative history advanced by some commenters.[228]

Next, NIEP defends the Commission's proposed findings that there is generally undue discrimination in the provision of transmission service. It notes that when an agency acts on an industry-wide basis, the agency does not have to make a finding as to each particular case.

Finally, NIEP responds to those who argue that AGD is not on point. It notes that the AGD court discussed electric cases and emphasizes the court's statement that the NGA "fairly bristles with concern for undue discrimination" -- a statement that is equally true of the FPA.

---

[228]NIEP explains that

(W)hile much has been made of the Senate report accompanying S.2114, which subsequently became part of PURPA in 1978, that report does not illustrate an intent to limit FERC's authority to remedy undue discrimination under Section 206. That report characterizes the Supreme Court's decision in Otter Tail as holding that "the Federal Power Act leaves open a gap in its failure to assign the FPC general authority to order wheeling in this situation * * *." The "situation" to which the Report refers is not discrimination, however. Instead, the statement appears to make reference to circumstances in which general public interest concerns, such as reliability, efficiency and competition, are at stake. Thus, Senate Report 2114 is simply not a limitation on the Commission's remedial powers under Sections 206.

NIEP Reply Comments at p. 8-9 (citations omitted).

TDU Systems responds to the argument that Otter Tail is a broad constraint on the Commission's authority to order transmission.[229] At issue in that case, it argues, was the reach of the Sherman Act, not of FPA sections 205 and 206. Similarly, it argues, the Florida Power case is not on point, and the court there specifically said that it was not deciding whether the Commission could have ordered wheeling as a remedy for anticompetitive activities. Moreover, TDU Systems asserts that EEI's use of a quote from a single Senator should carry no weight, since it is a well-established principle of statutory construction that such statements have little value. Finally, it points out that the AGD court itself did not view Otter Tail or other electric precedent as forbidding the Commission to order wheeling as a remedy for undue discrimination.

[31,676]

Entergy asserts that Congress's refusal to require utilities to provide transmission as common carriers or whenever it is in the public interest was merely a decision not to give the Commission general authority to order wheeling, without regard to undue discrimination. Thus, the Otter Tail language concerning the absence of a common carrier requirement does not demonstrate that Congress meant to limit the Commission's authority to remedy undue discrimination.

ELCON disputes EEI's reading of NYSEG, noting that the NYSEG court explicitly stated:

---

[229]See also Entergy.

Nor do we suggest that the Commission is powerless to review a wheeling agreement under 206 without following the requirements of sections 211 and 212.[230]

TAPS discusses numerous cases, including the primary cases relied upon by the Commission, and disposes of NYSEG by stating that it is no longer good law, if it ever was.

Commission Conclusion

There can be no question that the Commission has the authority to remedy undue discrimination. Sections 205 and 206 of the FPA mandate that we ensure that, with respect to any transmission in interstate commerce or any sale of electric energy for resale in interstate commerce by a public utility, no person is subject to any undue prejudice or disadvantage. Under these sections, we must determine whether any rule, regulation, practice, or contract affecting rates for such transmission or sale for resale is unduly discriminatory or preferential, and we must disapprove those contracts and practices that do not meet this standard. Our discretion is at its zenith in fashioning remedies for undue discrimination.[231]

Some commenters, however, challenge our authority to order industry-wide non-discriminatory open access as a remedy for the undue discrimination we have found in the

---

[230]ELCON Initial Comments at p. 7 (quoting NYSEG at 403).

[231]See, *e.g.*, Niagara Mohawk Power Corporation v. FPC, 379 F.2d 153, 159 (D.C. Cir. 1967).

industry. As summarized above, they essentially assert that we are prohibited by court precedent, the legislative history of the FPA, and sections 211 and 212 of the FPA from ordering wheeling as a remedy for undue discrimination. We disagree and conclude that we have the authority -- indeed, a responsibility -- to require non-discriminatory open access transmission as a remedy for undue discrimination.

AGD and Legislative History

The court decision in Associated Gas Distributors v. FERC provides powerful support for our ability to order industry-wide non-discriminatory open access transmission in the electric industry as a remedy for undue discrimination. As discussed in detail above, AGD, which is the only decision to have addressed the Commission's authority to remedy undue discrimination by requiring open access, upheld our authority under section 5 of the NGA (the parallel to section 206 of the FPA) to require open access in the natural gas industry. The rationale supplied by the AGD court applies equally to the FPA and our responsibility to eliminate undue discrimination in the electric industry.

Those who challenge the Commission's legal authority to remedy undue discrimination face the same difficulty that parties faced in seeking to overturn open access in the natural gas industry -- they "can point to no language in the (FPA) barring the Commission from imposing common carrier status on (public utilities), and certainly none barring it from imposing upon the (public utilities) a specific duty that happens to be a typical or even core component of such

status."[232] Instead, as was unsuccessfully attempted in the AGD proceeding, they seek to overcome the statutory silence primarily by means of legislative history. However, as the AGD court explained, legislative history is not even relevant, because

courts have no authority to enforce principles gleaned solely from legislative history that has no statutory reference point.[233] Here, as the court found with respect to the NGA, the legislative history of the FPA "provides strong support only for the point that Congress declined itself to impose common carrier status on (public utilities) * * * It affords weak -- **[31,677]** almost invisible -- support for the idea that the Commission could under no circumstances whatsoever impose obligations encompassing the core of a common carriage duty."[234]

Commenters focus on the following statement in the AGD decision to support the argument that, because Congress did not expressly reject common carriage under the NGA, but did reject it under the FPA, a different outcome in this proceeding is required:

we note that the legislative history of the two acts is, on this point, materially different. In its deliberations on the bill that

---

[232]AGD, 824 F.2d at 997.

[233]*Id.* (quoting IBEW, Local No. 474 v. NLRB, 814 F.2d 697, 712 (D.C. Cir. 1987)(emphasis deleted by court from original)).

[234]*Id.* (emphasis added).

ultimately emerged as the Federal Power Act, Congress considered and rejected a provision that would have "empowered the Federal Power Commission to order wheeling if it found such action to be 'necessary or desirable in the public interest.'" (citing Otter Tail) (quoting S. 1725, 74th Cong., 1st Sess.). The evidence as to the NGA (surveyed above) is less direct: it consists exclusively of various occasions on which Congress did not adopt proposals actually making the natural gas pipelines into common carriers.[235]

The above statement, however, does not preclude the AGD court's decision on our broad authority to remedy undue discrimination in the gas industry from applying equally in the electric industry. Clearly, the court did not say that. As discussed below, we believe the statement focuses on a distinction in the legislative histories that is not meaningful.

First, whether or not a material difference exists in the respective legislative histories of the NGA and FPA, the fact remains that the crucial findings of the AGD court were that: (1) "Congress declined itself to impose common carrier status" (emphasis added) and (2) there is no "support for the idea that the Commission could under no circumstances whatsoever impose obligations encompassing the core of a common carriage duty."[236] These findings apply equally to the

---

[235]*Id.* at p. 998-99.

[236]*Id.* at p. 997. We also note that the contract carriage obligation we are imposing is easily distinguished from the common carrier obligation Congress chose not to adopt. As discussed infra, the common carrier provisions rejected by Congress would have required transmission for "any person" upon reasonable request.

FPA. Simply stated, statutory silence cannot be overcome by means of legislative history -- even if the legislative history in fact indicated that Congress "rejected" legislative imposition of common carrier status under the FPA, but "did not adopt" it under the NGA. In either event, nothing in the statute or legislative history suggests that Congress concluded that the Commission could under no circumstances impose open access as a remedy to undue discrimination.

Moreover, the legislative history of the bills containing the FPA and the NGA, taken as a whole, suggests that the distinction drawn in AGD between the legislative histories of the NGA and the FPA is not meaningful. The legislation that was to become the FPA originally included provisions regulating both electric power and natural gas. As originally proposed, the legislation contained identical common carriage language for both public utilities and natural gas pipelines.

With respect to the FPA, the Supreme Court explained in Otter Tail that (a)s originally conceived, Part II would have included a "common carrier" provision making it "the duty of every public utility to * * * transmit energy for any person upon reasonable request * * *." In addition, it would have empowered the Federal Power Commission to order wheeling if it found such action to be "necessary or desirable in the public interest." H.R. 5423, 74th Cong., 1st Sess.; S. 1725, 74th Cong. 1st Sess. These provisions were eliminated to preserve "the voluntary action of the utilities." S.Rep. No.

This would have included retail purchasers.

621, 74th Cong., 1st Sess., 19.[237] The language paraphrased by the Supreme Court was from Title II of the initial bill proposing the Public Utility Holding Company Act. The entire sections from which the paraphrased language came are as follows:

SEC. 202. (a) It shall be the duty of every public utility to furnish energy to, exchange energy with, and transmit energy for any person upon reasonable request therefor; and to furnish and maintain such services and facilities as **[31,678]** shall promote the safety, comfort, and convenience of all its customers, employees, and the public, and shall be in all respects adequate, efficient, and reasonable.

* * *

SEC. 203. (b) Whenever the Commission after notice and opportunity for hearing finds such action necessary or desirable in the public interest, it may by order direct a public utility to make additions, extensions, repairs, or improvements to or changes in its facilities, to establish physical connection with the facilities of one or more other persons, to permit the use of its facilities by one or more other persons, or to utilize the facilities of, sell energy to, purchase energy from, transmit energy for, or exchange energy with, one or more other persons. Where any such order affects two or more persons, the Commission may prescribe the terms and conditions of the arrangement to be made between such persons, including the apportionment of

---

[237]Otter Tail, 410 U.S. at p. 374.

cost between them and the compensation or reimbursement reasonably due to any of them.[238]

This initial bill proposing the Public Utility Holding Company Act also included a Title III that was intended to regulate the transmission and sale of natural gas. Sections 303(a) and 304 of Title III included the identical common carrier language paraphrased by the Supreme Court and included in sections 202(a) and 203(b) of Title II.[239] After further deliberations, Congress rejected the above-quoted language in Title II and eventually adopted a Title II that did not include any common carrier language. On the other hand, Title III (addressing regulation of natural gas) was not reported out of committee, but reemerged in the next year.[240]

---

[238]H.R. 5423, 74th Cong., 1st Sess., 32 (emphasis added).

[239]*Id.* at p. 44.

[240]In the debate on the subsequent bill to regulate natural gas, Congressman Cole explained:

Mr. Chairman, the House should realize that the measure we are dealing with today is of extreme importance, more so than the attendance and the time taken in the discussion would seem to indicate. It is the culmination of one of the most far-reaching, intensive studies of the Federal Trade Commission I assume that that Commission ever conducted, and last year found a place in not identical language but very similar in the Rayburn bill, the famous holding-company bill, as part 3 thereof. Our committee eliminated part 3, as members will recall, and saved it for a separate measure reported out as it was last year, which was not considered by the House, but is here today in improved form. 81 Cong. Rec. H6724 (daily ed. July 1, 1937).

The bill that reemerged did not contain the common carrier language that was in the original Title III. However, as Congress had just debated the common carrier issue in enacting electric power regulation, it is not surprising that Congress did not engage in debating the very same issue in enacting natural gas regulation.

Because of the timing of the legislation involving the FPA and the NGA and the logical nexus between the two acts, we conclude that there is in fact no material difference as to this issue in the legislative histories of the two acts. Both initially included identical common carrier language, and the language was removed from both. As to both acts, Congress chose not to impose common carrier obligations on the electric or natural gas industries, but gave the Commission the authority and responsibility to eliminate undue discrimination in both industries. Consequently, as open access was found to be a proper remedy for undue discrimination in the natural gas industry, it is also a proper remedy for undue discrimination in the electric industry.

As the AGD court noted with respect to the Commission's powers and duties under the NGA, Congress explicitly gave the Commission the authority to eradicate undue discrimination under the FPA. That explicit power and duty provided by Congress cannot be invalidated solely on the ground that Congress chose not to impose statutory common carrier status on public utilities or did not explicitly authorize the Commission to do so.[241] As the AGD court explained, this would "turn[] statutory construction upside down, letting the

---

[241]AGD, 824 F.2d at p. 998.

failure to grant a general power prevail over the affirmative grant of a specific one."[242]

[31,679]
Other Case Law

A number of commenters argue that the Commission misinterpreted the other cases discussed in the NOPR with respect to our authority to order non-discriminatory open access transmission. We disagree. As demonstrated above, not one of the cases put forth by commenters holds that we cannot remedy undue discrimination by requiring public utilities to provide non-discriminatory open access transmission.[243]

AGD is the only case in which a court specifically addressed our authority to order open access transmission as a remedy for undue discrimination. Its favorable finding with respect to our action under section 5 of the NGA directly supports our ordering non-discriminatory open access transmission under section 206 of the FPA. Authority to Act by Rule

We disagree with those commenters that assert that we may find and remedy undue discrimination only through case-

---

[242]*Id.*

[243]See *FERC Statutes and Regulations* at p. 33,053-56. We further note that the AGD court did not discuss the NYSEG decision at all. Indeed, the NYSEG case did not involve any allegations of undue discrimination and any discussion of section 206 by the court was dictum.

by-case adjudications and are prohibited from making a generic determination of undue discrimination through a rulemaking. First, there is no question that it is within our discretion whether we act through rule or through case-by-case adjudications.[244] The AGD court specifically rejected a similar argument that the Commission erred in requiring open access transportation tariffs without first finding that each individual pipeline's rates were unlawful. The AGD court held that "(t)he Commission is not required to make individual findings if it exercises its §5 authority by means of a generic rule."[245]

We have identified a fundamental generic problem in the electric industry: owners, controllers and operators of monopoly transmission facilities that also own power generation facilities have the incentive to engage, and have engaged, in unduly discriminatory practices in the provision of transmission services by denying to third parties transmission services that are comparable to the transmission services that they are providing, or are capable of providing, for their own power sales and purchases. These practices

---

[244]*See, e.g., NLRB v. Bell Aerospace Company*, 416 U.S. 267, 293 (1974) (citing *SEC v. Chenery Corporation*, 332 U.S. 194, 202-03 (1947). *See also Heckler v. Campbell*, 461 U.S. 458, 467 (1983) (even where enabling statute requires a hearing to be held, agency may rely on its rulemaking authority); *Panhandle Eastern Pipeline Company v. FERC*, 907 F.2d 185, 187-88 (D.C. Cir. 1990). Under section 403 of the DOE Act, 42 U.S.C. 7173, the Commission is authorized at its discretion to initiate rulemaking proceedings.

[245]AGD, 824 F.2d at p. 1008.

drive up the price of electricity and hurt consumers. Furthermore, the incentive to engage in such practices is increasing significantly as competitive pressures grow in the industry. It is within our discretion to conclude that a generic rulemaking, not case-by-case adjudications, is the most efficient approach to take to resolve the industry-wide problem facing us.

b. Undue Discrimination/Anticompetitive Effects Initial Comments

A number of commenters allege that the Commission has failed to meet its burden of proving industry-wide discrimination.[246] They assert that the Commission has provided only a few unsubstantiated allegations of discrimination, which do not represent the current conditions in the electric industry, or that the Commission has not shown that all electric utilities have unduly discriminated. Some attack the NOPR's incorporation by reference of the unsubstantiated allegations of discrimination set forth in a petition for rulemaking filed on February 16, 1995 by the Coalition for a Competitive Electric Market (CCEM).[247]

EEI argues that the allegations of discrimination in the NOPR must be considered in light of the fact that: (1) all tariffs currently on file have been found by the Commission not to be discriminatory; (2) more than 30 utilities have voluntarily filed open access tariffs, which belies any

[246]E.g., EEI, Ohio Edison, PA Com, BG&E, NY Com, Minnesota P&L, Carolina P&L.

[247]E.g., EEI, BG&E.

assertion of widespread discrimination in the industry; and (3) transmission disputes are rare, with only 19 **[31,680]** section 211 proceedings having been filed in the last three years.[248] EEI concludes that the Commission's allegations of discrimination do not rise to the level of "extreme circumstances" found by the court in the natural gas industry in AGD.

EEI adds that the Commission's proposal to act under section 206 is itself discriminatory because it applies only to public utilities and does not reach all transmission-owning utilities.[249] If reciprocity is designed to resolve this problem, EEI believes that reciprocity should also be "effective for public utilities." Furthermore, EEI argues that the failure of a public utility to provide to others a service that it does not provide itself is not evidence of discrimination, and that inclusion of such a provision actually results in preferential treatment for transmission users.

NE Public Power District alleges that the NOPR does not contain a single reference to any actual discrimination or anticompetitive conduct by any publicly owned utility.

Salt River asserts that the Commission is required to consider all elements of an antitrust analysis before reaching a conclusion that market power exists in the transmission

[248]See also Ohio Edison.

[249]See also SCE&G.

system and that we have failed to do so.[250] It concludes that the NOPR "constitutes an attempt to legislate a remedy for an evil that has not been, and cannot be, lawfully found to exist on a wholesale basis among utilities that own and operate integrated generation and transmission systems."[251]

PA Com argues that the Commission's request for examples of discriminatory behavior is a "tacit admission as to the paucity of evidence of discriminatory practices by transmission owning utilities." NY Com argues that the "Commission's lack of a record basis for its proposed findings is legally suspect because courts in two cases have held that the Commission cannot proceed with open access transmission tariffs absent record findings of specific anticompetitive conduct."[252]

Finally, EEI claims that even if the Commission has proven its allegations of discrimination, we have failed to meet the requirements of section 206 of the FPA.[253] According to EEI, the Commission cannot find, without an adjudicatory hearing, that the rates on file are unlawful and

---

[250]Salt River Initial Comments at p. 5-6 (referencing an attached legal memorandum of Donald A. Kaplan).

[251]Salt River Initial Comments at p. 6.

[252]NY Com Initial Comments at p. 1 FLA-PAGE CITIATION ?6-18 (discussing FPL and Cajun).

[253]See also Southern.

order replacement rates.[254] The Commission's proposed procedure would unlawfully place the burden of justifying existing rates on the utilities.

Reply Comments

A number of commenters provide instances of discriminatory behavior they have faced over the years. NCMPA describes difficulties it has faced in dealing with CP&L, including a situation where CP&L allegedly impeded NCMPA's use of transmission access through CP&L's control of dispatching.[255]

AMP-Ohio alleges that Toledo Edison refused to transmit emergency power on a buy-sell basis to certain AMP-Ohio members even though Toledo Edison's system was not constrained. Instead, AMP-Ohio alleges, Toledo Edison bought the power and resold it to AMP-Ohio at a higher rate.

APPA challenges EEI's claim that there is no substantial evidence of undue discrimination in transmission. It suggests that nineteen instances of transmission disputes being filed since the Energy Policy Act was enacted is ample evidence of undue discrimination. Moreover, according to APPA, reported abuses are only the tip of the iceberg.

CCEM responds to the argument raised by EEI and others that there is no showing of extreme circumstances of

---

[254]See also Southern.

[255]We note that CP&L raised legal objections to our authority to implement this rule.

discrimination in the electric industry such as the AGD court noted in the gas industry. It says that these circumstances are present and gives numerous examples; it does not identify the specific utilities because "it is the experience of * * * (our) members that nearly all transmission owners retaliate **[31,681]** * * *" against anyone who complains. Moreover, in answer to EEI's statement that transmission disputes are rare, CCEM states that since most of the competition is in the short-term market, it has not been worthwhile to file complaints. The examples provided by CCEM include: (1) refusal by a California public utility to offer firm service; (2) refusal by control area utilities in Texas to offer ancillary services to a power marketer, with the result that one of the utilities won the bid, even though it did not have the lowest price; (3) non-utilities in ERCOT being unable to compete to meet short-term requests for economy energy because they were required to schedule by noon of the preceding day, while utilities did not subject themselves to such a scheduling requirement; (4) power pool or control area information requirements, particularly in the northwest part of WSPP, that force non-utilities to reveal commercially sensitive information; the transportation operator has then revealed the information to its own or its affiliate's sales arm, which "steals" the deal; (5) a northeast power pool that refused to wheel out even though capacity was available on the grounds that sending power out of the pool would drive up prices in the pool (hoarding); (6) a power marketer that asked a utility to provide transmission, whereupon the utility bought up certain transmission capacity necessary for the marketer to reach its buyer, thus blocking the path -- this was possible because the utility was able to locate the purchaser based on commercially sensitive information the marketer had to give the utility when the marketer asked for transmission; (7) a common contracting

practice among utilities restricting the use of interconnections to themselves, particularly in the Southwest Power Pool, MAPP, and MAIN; (8) utilities overstating the cost of improvements (gold-plating) and thus discouraging service. CCEM also responds to each of EEI's criticisms of CCEM's examples of undue discrimination submitted in its February 16, 1995 petition and argues that its examples of undue discrimination are unrebutted.

Brownsville asserts that

while PUB [Brownsville] must pay multiple distance-based and pancaked transmission rates to engage in transactions with the non-ERCOT universe, El Paso Electric would have received transmission payments from its merger partners while gaining free transmission access to buy and sell within ERCOT. CSW presently walls other ERCOT utilities off from participation in the Western Systems Power Pool, while its ERCOT subsidiaries, CPL and WTU, share in the benefits of their non-ERCOT affiliates' WSPP memberships via the preferential terms of the CSW Operating Agreement. CSW treats its own inter-affiliate central dispatch as having a higher priority than third-party economy energy transactions, with the result that CPL not infrequently crowds PUB out of the economy market.[256]

Wisconsin Municipals states that its members have been fighting transmission battles for years and sets forth five examples of the sort of difficulties it has experienced in

---

[256]Brownsville Reply Comments at p. 2-3 (emphasis in original).

attempting to obtain transmission rights. For example, it explains that Wisconsin public utilities have resisted an effort by the state commission to achieve comparability of use of transmission. Wisconsin Municipals also explains a situation where "if WPPI continued to purchase its power from WPSC, it would pay WPSC $843,840 annually for transmission service: if it purchases power off system from WP&L (one of WPSC's competitors), WPPI would pay WPSC $1,774,224 for transmission service to the exact same load."

TAPS sets forth additional examples of undue discrimination, including refusals to wheel even in the face of Nuclear Regulatory Commission (NRC) nuclear license conditions requiring wheeling, and Northeast Utilities' refusal to provide transmission to a QF even though it had indicated to the Commission that it would provide such transmission in order to obtain Commission approval of its proposed merger with Public Service Company of New Hampshire.

NIEP sets forth ten examples of undue discrimination that its members have experienced in seeking access to transmission service at reasonable terms and conditions.

[31,682]

Some commenters challenge these claims of undue discrimination. For example, Carolina P&L responds to NCMPA #1's example of obstruction by Duke in accommodating energy sales from the jointly owned Catawba Plant. Carolina P&L explains that NCMPA #1's proposal "would require Duke to provide its own generation resources on behalf of NCMPA #1 in order to support a bulk power sale when NCMPA #1's own resource capacity and energy are not sufficient for the sale." Carolina P&L argues that this is

backstanding that goes beyond the scope of any ancillary service the Commission has proposed and would be entirely inappropriate "to compel the Transmission Provider to sell power to its Transmission Customer for resale on the bulk power market."

Duke also responds to NCMPA #1's claim of discrimination and asserts that NCMPA #1's claim is not relevant to the NOPR proceeding, but is a specific contractual claim that should be pursued pursuant to the terms of its contract.

Commission Conclusion

We conclude that unduly discriminatory and anticompetitive practices exist today in the electric industry and, more importantly, that such practices will increase as competitive pressures continue to grow in the industry, unless the Commission acts now to prevent such practices.[257] It is in the economic self-interest of transmission monopolists, particularly those with high-cost generation assets, to deny transmission or to offer transmission on a basis that is inferior to that which they provide themselves. The inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own

---

[257]While many public utilities have filed some form of open access tariff (often in response to our proposed rule), we believe that many of the remaining utilities will not voluntarily open their systems absent a final rule. See also note 266.

generation, and it is our duty to eradicate unduly discriminatory practices. As the AGD court stated: "Agencies do not need to conduct experiments in order to rely on the prediction that an unsupported stone will fall."[258]

We set forth examples in the NOPR of undue discrimination that we believe are occurring in the electric industry and invited commenters to identify any discrimination that they may have experienced. In response, commenters presented numerous additional examples of undue discrimination, which are summarized above, and we set forth below further examples of undue discrimination that have been raised in cases before the Commission.

Many of the examples of discriminatory behavior that have been brought to our attention do not name the specific utilities involved, and many are allegations that are not proven. However, we do not believe that this undermines our finding of unduly discriminatory practices by transmission owners and controllers. We believe that it is only natural that potential transmission customers with an interest in participating in electric markets will be reluctant to name names for fear of being shut out of those markets. CCEM, which identified a wide array of discriminatory behavior its members have experienced, explained that

(w)e do not identify the specific utilities in each example because it is the experience of CCEM members that nearly all transmission owners retaliate by cutting off all communications with anyone that challenges or complains

[258]AGD, 824 F.2d at p. 1008.

about the rates, terms or conditions at which the owner offers access to its system. Inasmuch as most of the competitive commerce in electric power today is in short-term markets, it is typically not worth the effort of CCEM members or other transmission-dependent entities to file a complaint with the Commission's enforcement staff or in the courts in connection with a transmission owner's discriminatory practices. The deal is lost well before a complaint can be processed and ruled upon.[259]

Other examples of discriminatory behavior have also been raised in proceedings before the Commission. As we **[31,683]** explained in detail in the NOPR, transmission-owning utilities have discriminated against others seeking transmission access in a variety of ways, most often subtly and indirectly.[260] For example, delaying tactics have been used to frustrate access. The history of Pacific Gas and Electric Company's (PG&E) attempt to avoid its commitments made to the California owners of the California-Oregon Transmission Project (COTP) is a prime example. The owners had originally planned the COTP to have its southern terminus at the Midway station with Southern California Edison. PG&E convinced them to terminate the project instead at PG&E's Tesla station and indicated that PG&E would provide transmission service the rest of the way south to Midway. PG&E promised this service in 1989 (in Principles). PG&E spent the next four years filing substitute

[259]CCEM Initial Comments at p. 18-19. See also NIEP Reply Comments at p. 13 n.31.

[260]*FERC Statutes and Regulations* at p. 33,072.

provisions for what it had promised in the Principles.[261] Additional allegations of discriminatory behavior are set forth in Appendix C, which includes allegations made under oath in proceedings at the Commission and allegations made in pleadings and other documents before the Commission.

In addition, to date, the Commission has received 28 section 211 transmission requests.[262] Applicants submit section 211 transmission requests when the transmission provider refuses to provide the requested transmission service. For example, American Municipal Power-Ohio, Inc. (AMP-Ohio) requested Ohio Edison Company (Ohio Edison) to establish additional delivery points to certain of AMP-Ohio's members and to permit the addition of delivery points in the future upon AMP-Ohio's request. Ohio Edison refused AMP-Ohio's request, claiming that it was not a proper request under section 211 because it already provided wholesale transmission to the municipal utilities at issue. In a proposed order, the Commission disagreed with Ohio Edison and ordered Ohio Edison to provide the requested additional

---

[261]*See Pacific Gas and Electric Company*, 65 FERC ¶61,312 at p. 62,428-30 and n.22, remanded on other grounds, *Pacific Gas & Electric Company v. FERC*, No. 94-70037 (9th Cir. June 23, 1994)(unpublished opinion), order on remand, 69 FERC 61,006 (1994).

[262]A list of section 211 applications and the status of each is attached as Appendix A.

delivery points and to entertain future requests by AMP-Ohio for specific delivery points.[263]

Many of the examples of discriminatory actions we are seeing in the electric industry are similar to those we saw in the gas industry. Given our experience, we find that these examples of discriminatory actions are credible and well-founded. Thus, we conclude that there is more than sufficient reason to believe that transmission monopolists currently engage in unduly discriminatory practices, and that they will continue to engage in unduly discriminatory practices, unless we fashion a remedy to eliminate their ability and incentive to do so. In light of the competitive changes occurring in today's electric industry, we believe that the only effective remedy is non-discriminatory open access transmission, including functional unbundling and OASIS requirements, and that it is within our statutory authority to order that remedy.

Further, we disagree with the argument that we are limited to applying a traditional antitrust analysis in determining whether market power exists in the transmission system. While we must take antitrust concerns into consideration in exercising our responsibilities under the FPA, we are not an antitrust court, and our responsibilities are not those of the Department of Justice.[264] We have

---

[263]*American Municipal Power-Ohio, Inc. v. Ohio Edison Company*, 74 FERC ¶61,086 (1996).

[264]*See, e.g., Gulf States Utilities Company v. FPC*, 411 U.S. 747, 758-60 (1973); *FPC v. Conway Corporation*, 426 U.S. 271, 279 (1976); *Northern Natural Gas Company v. FPC*, 399 F.2d 953, 960 (D.C. Cir. 1968).

analyzed the incentives and practices of monopoly transmission owners and controllers in light of the statutory standards and directives of the FPA and, based on our findings, have properly concluded that there is a generic problem that must be remedied.

The Commission also recognizes, as some commenters suggest, that we have, in the past, permitted utilities to file tariffs containing restrictions on transmission **[31,684]** service that we are now finding to be unduly discriminatory in this rule and that we found unduly discriminatory in cases since our decision in AEP. However, it is entirely appropriate, and indeed necessary, that our application of the FPA's undue discrimination standard evolve over time and adapt to the changing circumstances in the industry. Our prior willingness to tolerate the use of monopoly power over transmission to maintain and aggregate the utility's market power over generation occurred in the context of an industry structured largely as vertically integrated regulated monopolies that supplied all facets of utility service -- power supply, transmission, and distribution -- as a single monopoly service. Competition generally was not meaningfully available as a means to discipline prices and consumer interests were best served by improving efficiencies of the integrated utilities, subject to cost-based regulation.

Today, the circumstances of the industry are radically different. As explained in detail in Section III, a series of significant economic, regulatory, and technical changes in the power industry has introduced the promise of competitively priced power supplies. The profile of electric power suppliers has expanded to include not just the power supply arms of traditional utilities, but also independent power suppliers,

affiliated utility power suppliers selling into territories of other franchise utilities, and power marketers.[265] This offers the promise of an increasingly competitive commodity market in electric power, in which significant benefits to consumers can be achieved. In the context of an emerging competitive market in generation, discriminatory practices that once did not constitute undue discrimination must be reviewed to determine whether they are being used to prevent the benefits of competition in generation from being achieved. Here we find conclusively that they are, and use our remedial authority to ensure that they can no longer occur.[266]

---

[265]We note that there are now 14 power marketers that are affiliated with public utilities.

[266]We take note of EEI's comments that, at the time of the comments, 30 utilities had filed open access tariffs. They argue, therefore, that the rule is unnecessary. Since their comment was filed, the number of utilities filing some form of an open access tariff has risen to 106. However, while some of these tariffs are based on the NOPR pro forma tariffs, many of these tariffs fall significantly short of the tariff requirements of both the NOPR and this Rule. Even if the tariffs met these requirements, the Rule is still needed to complete the task of eliminating undue discrimination by all public utilities and assuring, to the extent possible, a nationwide open access transmission grid. Indeed, a number of these tariffs were filed for the purposes of securing authority to market power competitively. This underscores markedly our fundamental conclusion that prior practices of using monopoly power over transmission to preserve market power over electricity sales has no place in today's industry and must be eliminated to get the benefits of competition to the customers we are required to protect under the FPA.

* * * * *

[pp. 31,687 - 31,703]

[31,687]

C. *Comparability*

1. Eligibility to Receive Non-Discriminatory Open Access Transmission

In the NOPR, the Commission proposed to define who is eligible to receive service under a non-discriminatory open access tariff as follows:

A non-discriminatory open-access tariff must be available to any entity that can request transmission services under section 211.[281]

The Commission further explained that "[u]nder section 211, any electric utility, Federal power marketing agency, or any other person generating electric energy for sale tot resale may request transmission services under section 211."[282]

PSNM believes that the NOPR properly defined customer eligibility. NIEP, on the other hand. believes that the posed definition is too limited. It argues that the Commission should require public utilities to make transmission service available to all entities engaged in

[281] *FERC Statutes and Regulations P* 32,514 at p. 33,083 (footnote omitted)

[282] *Id.* at p. 33,083 n.195.

wholesale purchases or sales of power, not just to those "generating" power. Utility Working Group requests that the Commission **[31,688]** clarify that eligibility is dependent not only on being the type of entity set forth in section 21I, but on meeting the requirements of section 212(h) (Prohibition on Mandatory Retail Wheeling and Sham Wholesale Transactions) as well.[283]

We also received several comments related to the applicability of the rule to foreign entities. Canada states that the requirements for comparability and reciprocity should be implemented in a flexible masher to permit Canadian utilities to have fair and competitive access in the U.S. electricity market. Maritime requests that the Commission require Canadian utilities who wish to participate in the U.S. market to offer other utilities the same privileges they receive in the United States. Southwestern argues that transmission to a foreign country is in interstate commerce and that a utility should therefore accommodate this type of transmission request under its open access tariff. El Paso argues that the Commission does not have the authority to condition access to foreign countries, but states that if the Commission nevertheless exercises such authority it should do so on a case-by-case basis, Destec asserts that the posturing of Ontario Hydro before U.S. regulators pleading for open access and non-discriminatory transmission treatment – even for extra-territorial entities, should be met with a strong reply that such provisions should also be afforded transmission dependent entities on the Canadian side of the border. Ontario

[283] Section 212(h) (Prohibition on Mandatory Retail Wheeling and Sham Wholesale Transactions).

Hydro's aggressive pursuit of U.S. market opportunities while simultaneously blocking competitors through the control o£ their transmission assets can not be ignored. Commission Conclusion.

In the Final Rule pro forms tariff the Commission has modified the definition of "eligible customer" to address concerns that in some respects the NOPR definition was too limited and in other respects it was too broad. This includes amended language to clarify that any entity engaged in wholesale purchases or sales of energy, not just those "generating" electric power, is eligible. It also includes clarification that entities that would violate section gig(h) of the FPA (prohibition on Commission-mandated wheeling directly to an ultimate consumer and sham wholesale transactions) are not eligible. The language also has been modified to provide that foreign entities that otherwise meet the eligibility criteria may obtain transmission services. Further, it has been modified to provide for service to retail customers in circumstances that do not violate FPA section 212(h).[284]

Persons that would be eligible section 211 applicants also would be eligible under the open access tariffs. Section 211 applicants may be any electric utility, Federal power marketing agency, or any other person generating electric energy for sale for resale.

---

[284]We emphasize that any transmission customer must follow prudent utility practices so to assure reliability.

Section 3(22) of the FPA. as amcnded by the Energy Policy Act, defines "electric utility" co mean any person or State agency (including any municipality) which sells electric energy; such term includes the 'Tennessee Valley Authority. but does not include any Federal power marketing agency. Thus, as we have previously noted, municipal utilities are electric utilities simply by the terms of the statute.[285] In addition, we have also found that cooperatives and marketers are electric utilities as defined in the FPA.[286] Other entities that fall within the definition include IOUs, IPPs, APPS, and QFs that sell electric energy.

We do not believe that entities that engage solely in brokering should be eligible. Such brokers do not take title to electricity and therefore do not engage in the sale of electric energy; nor do they generate electric energy for sale for resale.[287]

---

[285]New Reporting Requirement Implementing Section 213(b) of the Federal Power Act Supporting Expanded Regulatory Responsibility Under the Energy Policy Act of 1992, and conforming and Other Changes to Form No. FERC-714. Order No. 558-A, 65 FERC ¶61,324 at p. 62.451 n. 12 (1993).

[286]Order No. 558. *FERC Statutes and Regulations* ¶30,980 at p. 30,895-96, reh'g denied. 65 FERC ¶61,324 (1993) (cooperatives are electric utilities): *AES Power, Inc.*, 69 FERC ¶61,345 at p. 62.297 (1995) (power marketer is an electric utility, i.e., a person "which sels electric energy").

[287]*See, e.g., Citizens Energy Corporation*, 35 FERC ¶61,198 at p. 61.452-53 (1986).

[31,689]

Although such brokers are not eligible under the tariffs, they will be able to arrange deals because they will have access to the OASIS of all public utilities and will be able to solicit information from the relevant transmission service providers under the terms of the applicable tariffs.

We clarify that foreign entities that otherwise meet the eligibility criteria must be eligible to receive service under the non-discriminatory open access transmission tariffs.[288] We are making this determination pursuant to our authority under section 206 of the FPA to remedy undue discrimination. As we explained in the NOPR. market power through the control of transmission can be used discriminatorily to block competition. Customers in the United States should not be denied access to cheaper supplies of electric energy, whether such electric energy is from a domestic source or a foreign source. By making non-discriminatory access available to foreign entities that otherwise meet the eligibility criteria: we are assuring that customers in the United States have access to as many potential suppliers as possible. This should result in increased competition and lead to customers paying the lowest possible prices for their electric energy needs. To the extent that such an entity obtains access, however, we emphasize that it would be subject to all of the terms and conditions of the applicable open access tariff, including the requirement that it provide reciprocal service.

---

[288]In making this determination, we are not deciding whether these entities are eligible entities under section 211(a) of the FPA.

Finally, we have reconsidered our NOPR position that would have limited eligibility to wholesale transmission customers. As we explained in the NOPR. the Commission's jurisdiction, extends to all unbundled transmission, in interstate commerce by public utilities. It is irrelevant to the Commission's jurisdiction whether the customer receiving the un-bundled transmission service in interstate commerce is a wholesale or retail customer. Thus, if a public utility voluntarily offers unbundled retail access interstate commerce or a state retail access program results in unbundled retail access in interstate commerce by a public utility, the affected retail customer must obtain its unbundled transmission service under a non-discriminatory transmission tariff on file with the Commission. Though the Commission may approve a separate retail transmission tariff when some variation is necessary or appropriate to meet local concerns,[289] we generally see no reason why retail transmission tariffs necessarily must be different from wholesale transmission tariffs. For that reason, we anticipate that in .many circumstances the same open access tariff that serves wholesale customers will be equally appropriate for retail transmission customers. Therefore, unless the Commission has specifically permitted a separate retail tariff, eligible customers under the Final Rule pro forma

---

[289]See Section IV.I.

tariff must include unbundled retail customers,[290] We discuss this further in Section IV.I.

While the rates, terms, and conditions of all unbundled transmission service will be subject to a Commission-authorized tariff, we will, in appropriate circumstances, give deference to state recommendations regarding rates, terms, and conditions for retail transmission service or regarding the proper transmission cost allocation to be used between retail and wholesale customers when state recommendations are consistent with our open access policies. This is also discussed further in Section IV.I.

Moreover, we are mindful of the fact that we are precluded under section 212(h) from ordering or conditioning an order on a requirement to provide wheeling directly to an ultimate consumer or sham wholesale wheeling. We therefore clarify that our decision to eliminate the wholesale customer eligibility requirement does not constitute a requirement that a utility provide retail transmission service. Rather, we make clear that if a utility chooses, or a state lawfully requires, unbundled retail transmission service, **[31,690]** such service should occur under this tariff unless we specifically approve other terms.

---

[290]The Commission has no authority to order retail transmission directly to an ultimate consumer or to order "sham" wholesale transmission, See FPA section 212(h). However. if such access occurs voluntarily or as a result of a state program, the rates, terms, and conditions of the access are within our exclusive jurisdiction if the service is provided by a public utility.

2. Service That Must be Provided by Transmission Provider

In the NOPR, the Commission proposed that a public utility must offer to provide any point-to-point or network transmission service whether or not the utility provides itself that service:

The Commission therefore proposes that all public utilities must offer both firm and non-firm point-to-point transmission service and firm network transmission service on a nondiscriminatory open access basis in accord with the proposed rule and the attached appendix tariffs. The Commission believes that a utility's tariff must offer in provide any point-to-point transmission service and network transmission service that customers need, even though the utility may not provide itself the specific service requested.[291]

EGA and SMUD agree that a transmission owner should offer any transmission service it is able to provide, even if it does not use the service itself:

Public Generating Pool, an association of consumer-owned electric utilities, appears concerned that the Commission may interpret comparability broadly to require a utility to offer the same service provided by another utility or to offer service generally available in a region. Thus, it recommends that a third party seeking more service than a utility provides itself be required to resort to the section 211 process.

---

[291]FERC Statutes and Regulations ¶32,514 at p.33,079

Commission Conclusion

Initially, we note that, with the possible exception of small utilities (which may qualify for a waiver, see infra), we have seen no evidence that public utilities are incapable of reasonably providing the services required in the Final Rule pro forma tariff. Nor have we seen evidence that utilities able to provide these services to themselves are choosing to forego such services. In short, we are not convinced that there is an appreciable difference, if any, among the services required in the pro forma tariff, the services utilities are able to provide, and the services they actually provide themselves.

To the extent these services do differ, however, we explicitly adopt the proposal set forth in the NOPR. Thus, a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others. Because a public utility that is reasonably capable of providing transmission services may provide itself such services at any time it finds those services desirable, it is irrelevant that it may not be using or providing that service today. Moreover. a public utility must offer these transmission services whether or not other utilities may be able to offer the same services and whether or not such services are generally available in the region (waiver of these requirements for .small utilities is discussed in Section IV.K.2.).[292] However, if a customer seeks a customized service not offered in an open access

[292]Requirements for ancillary services are discussed in Section IV.D.

tariff, a customer may. barring successful negotiation for such service, file a section 211 application.

3. Who Must Provide Non-Discriminatory 0pen Access Transmission

In the NOPR, the Commission proposed to require all "public utilities" owning and/or controlling facilities used for transmitting electric energy in interstate commerce to file open access transmission tariffs.[293] We explained that we could not require all "transmitting utilities" to file open access tariffs under sections 205 and 206 because we do not have jurisdiction over non-public utilities under these sections.

Several commenters argue that the open access requirement must be applied to non-jurisdictional utilities that own interstate transmission facilities.[294] Power Marketing Association recognizes that this raises difficult legal issues and suggests that the Commission support legislation to expand the Commission's authority over non-jurisdictional utilities. Minnesota P&L argues that ir the requirement is not applied to all entities that own transmission, jurisdictional and **[31,691]** non-jurisdictional entities owning joint transmission facilities will be competitively disadvantaged due to unequal pricing. Union Electric argues that unless the requirement is extended to the 56 non-jurisdictional entities operating control areas, discrimination in the wholesale power markets will increase.

[293]*FERC Statutes and Regulations* ¶32,514 at p. 33,049.

[294]*E.g.*, Minnesota P&L, Power Marketing Association.

A number of municipal commenters assert that the NOPR overlooks transmission assets jointly owned by jurisdictional and non-jurisdictional utilities.[295] They argue that agreements regarding use of these assets often contain provisions prohibiting third-party power transfers. They further argue that such provisions should be nullified, and the joint owners should be required to develop equitable methodologies to allocate wheeling revenues among themselves.

Several cooperatives urge the Commission to clarify that contracts among their constituent cooperatives are not subject to any unbundling of existing contracts.

Commission Conclusion

Our authority under sections 205 and 206 of the FPA permits us to require only public utilities to file open access tariffs as a remedy for. undue discrimination. We have no authority under those sections of the FPA to require non-public utilities to file tariffs with the Commission.

However, we are concerned that if nonpublic utilities do not provide access, there will remain a patchwork of "open" and "closed" transmission systems and the potential for distortions in wholesale bulk power markets. We believe that certain mechanisms exist that will help to alleviate these problems.

---

[295]E.g., Springfield.

First, as we explained in the NOPR, broad application of section 211 will provide wider access to bulk power markets.[296] Under section 211, eligible entities may seek transmission service from "transmitting utilities," which section 3(23) of the FPA defines as "any electric utility, qualifying cogeneration facility, qualifying small power production facility, or Federal power marketing agency which owns or operates electric power transmission facilities which are used for the sale of electric energy at wholesale." We believe that section 211 provides us with authority to require the same quality of transmission service as sections 205 and 206, though the procedural path is more cumbersome. Thus, section 211 provides access to transmission systems owned or operated by non-public utilities.[297]

Second, as we explained in the NOPR, our reciprocity requirement is designed to provide the widest possible use of the nationwide transmission grid:

The purpose of this provision is to ensure that a public utility offering transmission access to others can obtain similar service from its transmission customers. It is important that public utilities that are required to have on file tariffs be able to obtain service from transmitting utilities that are not public

---

[296]*FERC Statutes and Regulations* ¶32,514 at p. 33,050 and 33,092-93.

[297]As discussed in the NOPR, sections 211 and 212 require that applicants specify only fates, terms, and conditions of service, not specify transactions. Thus, applicants can file requests for tariffs to accommodate future currently unspecified transactions, similar to the open access tariffs required by this Rule.

utilities, such as municipal power authorities or the federal power marketing administrations that receive transmission service under a public utility's tariff.[298]

Finally, again as we explained in the NOPR, the formation of RTGs should speed the development of competitive markets and involve more non-public utilities in the provision of non-discriminatory open access transmission.[299] In approving RTGs, our policy has been to require all members, whether or not they are public utilities, to offer comparable transmission services at least to other members.

We recognize that these solutions are not perfect. However, given the difficulties inherent in the statutory scheme, we believe they will go a long way toward effectuating transmission access by nonpublic utilities,

One further issue involving non-public utilities concerns jointly owned transmission facilities. We will not allow public utilities that jointly own interstate transmission **[31,692]** facilities with non-jurisdictional entities to escape the requirements of open access. We will require each public utility that owns interstate transmission facilities jointly with a non-jurisdictional entity to offer service over its share of the joint facilities, even if the joint ownership contract prohibits service to third parties. we urge such public utilities to seek mutually agreeable revisions to their agreements to permit

---

[298]*FERC Statutes and Regulations* ¶32,514 at p. 33,089.

[299]*Id.* at p. 33,095.

third-party access over all. or at least their share, of the facilities. For those joint ownership arrangements that include restrictions on the usage of jointly owned transmission facilities by third parties, we will require the public utilities, in a section 206 compliance filing. to file with the Commission, by December 31, 1996, a proposed revision (mutually agreeable or unilateral) to its contract with the non-jurisdictional owner(s). This revision must be designed at a minimum to permit third parties to use the public utility's share of the joint facilities in accordance with this Rule and must provide for any needed cost allocation procedures between the public utility and the non-jurisdictional owner(s).

4. Reservation of Transmission Capacity by Transmission Customers

In the NOPR, the Commission set forth the information that a requester of transmission service would have to submit with a service request. We recognized that there may have to be a limit, for competitive reasons, on the information required, but also recognized the need to assure that no customer would reserve scarce capacity and then hold it without using it.[300] To avoid forcing transmission customers to reveal unnecessary details of their purchase or sales transactions, the Commission discussed several less restrictive options: (1) Allow the transmission provider to use or sell the capacity while it is unused, (2) have a pool that clears the short-term market, and (3) require the customer to begin using the capacity within some specified period or lose its

---

[300]*Id.* at p. 33,090.

reservation rights. The Commission requested comments on these and other possible approaches.

Unused or Unneeded Transmission Capacity

Many commenters recommend a use-it-or-lose-it rule (i.e., a transmission customer must use its reserved transmission capacity or lose its rights to that capacity).[301] Several commenters also recommend a number of restrictions on capacity reservations to reduce incentives to hoard or to cherry-pick (request to reserve firm capacity only during peak hours of peak seasons) existing transmission capacity. These include: (I) Allow requesters to reserve a place in the queue with a right o[first refusal over later competing requests; (2) impost a take-or-pay charge on reservations and deny reservation holders the right to revenue sharing if they do not schedule or assign their rights; (3) limit the time period for reservations; (4) limit how far in advance reservations may be made for both non-firm and firm services: (5) maintain a price cap on the resale of transmission; (6) require multi-year reservations to be for sequential periods; and (7) require a nonrefundable fee for advance reservations of service.[302] Southwestern suggests that transmission tariffs include a provision that prevents transmission customers and the

---

[301]*E.g.*, Consumers Power, Northern States Power, PacifiCorp, Oklahnma G&E, Allegheny Power, ELCON, Public Service Co of CO.

[302]*E.g.*, Northern States Power, VEPCO, Utilities For Improved Transition, PacifiCorp, Arizona Public Service, Dairyland, Montaup, Illinois Power, South Carolina E&G, Florida Power Corp. KU.

transmission provider from reserving and tying up firm transmission capacity for speculative wholesale actions.[303]

On the other hand, PSNM believes that a use-it-or-lose-it approach is inappropriate because any prudent utility that has reserved capacity would seek to sell the service it is not using so as to recover some portion of its fixed costs. Wisconsin P&L argues that a use-it-or-lose-it approach would not work, would be difficult to administer, and may be anticompetitive.[304] Central Illinois Public Service asserts that a reservation holder has little incentive to hoard capacity because other customers can use the capacity on a non-firm basis during times when a reservation **[31,693]** holder does not schedule power. It warns that giving the transmission operator the ability to schedule unused capacity may result in undue influence and the exercise of market power. CA Energy Cpm maintains that, while reassignment would help prevent hoarding, it would not assure efficient use of the full transmission network,

Use of Pooling Arrangements To Prevent Improper Reservations

Allegheny Power contends that a pooling arrangement could provide an incentive to hoarders to release capacity during a shortage. It suggests that capacity could be auctioned within a pool pt available capacity. However, it acknowledges

---

[303]See also NRECA.

[304]Wisconsin P&L notes, however, that a possible exception exists where a user could block the efficient transfer of power and then market its own power at a premium price.

that an auction would be tantamount to allowing the network owner to sell transmission service at unregulated rates.

PacifiCorp does not believe that a pooling arrangement would prevent capacity hoarding unless nonsequential reservations are prohibited ELCON contends that a use-it-or-lose-it rule would be fairer and more effective than pooling.

Commission Conclusion

Upon further consideration, we conclude that firm transmission customers, including network customers, should not lose their rights to firm capacity simply because they do not use that capacity for certain periods of time. Firm transmission customers that have reserved capacity and paid a reservation charge generally do not use the entire amount of reserved capacity at all times. This does not mean, however, that they must permanently return the unused amount to the utility. In the absence of evidence of hoarding or other anticompetitive practices, we will not limit the amount of transmission capacity that a customer may reserve. Firm transmission customers are in the best position to know the levels of electric energy they will be transmitting and the level of flexibility they need in carrying out their transmission activities. Indeed, when they are not using their reserved capacity, firm transmission customers remain obligated to pay the utility a reservation charge that covers all of the utility's fixed costs associated with the reserved capacity.[305]

---

[305]A reservation charge would assure that the utility fully recovers its fixed costs associated with the transmission customer's reserved transmission capacity.

Moreover, the possibility that a customer will reserve capacity and then hold it without using or reassigning it is mitigated because the utility is free to schedule and sell any unscheduled firm point-to-point transmission capacity on a non-firm basis to any entity eligible to receive such service under the utility's tariff. We also note that it is in the economic self interest of reservation holders to make available unused capacity to the market.[306]

We recognize that situations could arise in which a customer unlawfully withholds capacity. That is, a transmission customer could retain capacity in a way that could have an anticompetitive effect. For example, a transmission customer may serve certain capacity simply to prevent everyone else From using it and to make its own generation the only alternative available to the market. However. as described above, we believe that the incentives are such that parties are more likely to release unneeded capacity and that a generic remedy is therefore unnecessary. Any substantial allegations that indicate that a transmission customer is withholding scarce capacity in a way that has an anticompetitive effect would be addressed under section 206. If we round such allegations to be true, we could order the customer to return the capacity reservation right to the transmission operator. This approach should allay concerns that a customer may reserve scarce capacity and nat use it, without forcing customers to demonstrate need or to reveal details of individual transactions.

---

[306]See Section IV.C.6.

5. Reservation of Transmission Capacity for Future Use by Utility Comments

EEI and many IOUs argue that native load and network transmission customers should have first priority to existing capacity for their reasonably forecasted load requirements because that capacity was constructed to provide service to them and was paid for by them.[307] EEI contends that such priority ensures **[31,694]** equity and comparability based on past and future cost responsibility for the system. Similarly, Florida Power Corp and PECO contend that third-party customers should not be allowed to use transmission capacity that native load customers would grow into within a reasonable planning horizon.

Other commenters disagree, asserting that available transmission capacity must be determined in the same manner for all customers and that utilities should not be permitted to reserve capacity for their own uses.[308] NIEP argues that utilities should not be permitted to lock up available transmission capacity over valuable transmission paths and then require transmission requesters to pay for the cost of incremental transmission upgrades. This would let the utility avoid incremental transmission charges on its system.

---

[307] *E.g.*, NYPP, Public Service E&G, Sierra Pacific Power, Ohio Edison, Sierra Pacific Power asserts that a utility should be permitted to retain capacity for native load use over the pertinent planning period. El Paso adds that the Commission should allow utilities the opportunity to reserve capacity for anticipated uses that, although not firm, are necessary to maintain reliability.

[308] *E.g.*, NIEP, CCEM, Conservation Law Foundation.

Oklahoma G&E argues that existing available transmission capacity should be made available until it is needed for native load growth. Utilicorp states that transmission owners should not be permitted to set aside capacity for sales or purchases of economy energy. CCEM argues that the centerpiece of comparability is that ail transmission customers, including the merchant operations of the transmission owner, take service from available capacity pursuant to the same tariffs. CCEM .adds that allowing utilities to reserve capacity based on forecasted retail and network loads creates an incentive for them to over-forecast their load to the detriment of all others. NRECA suggests that the need to maintain reliability should not perpetuate transmission providers' preferential treatment of their own transactions. It also recommends that, during periods when facilities are constrained, access be allocated based on a combination of past actual use and planned future use.

Commission Conclusion

We conclude that public utilities may reserve existing transmission capacity needed for native load growth and network transmission customer load growth reasonably forecasted within the utility's current planning horizon. However, any capacity that a public utility reserves for future growth, but is not currently needed, must be posted on the OASIS and made available to others through the capacity reassignment requirements, until such time as it is actually needed and used.

In response to arguments raised by several commenters that existing requirements customers should have future right to existing capacity beyond the terms of their contracts

because of their historical use, as discussed previously, we believe existing customers should have a right of first refusal to capacity they previously used. if they are willing to match the rate offered by another potential customer, up to the transmission provider's maximum filed transmission rate at that time, and to accept a contract term at least as long as that offered by another potential customer.[309]

6. Capacity Reassignment

In the NOPR, the Commission proposed that a tariff must explicitly permit reassignment of firm service entitlements.[310] We explained thai reassignment of capacity rights could have a number of benefits: (1) Helping transmission users manage financial risk. (2) reducing transmission providers' market power by enabling transmission customers to compete with them, and (3) improving capacity allocation when capacity is constrained and some market participants value capacity more than current capacity holders. We requested comments on whether the current price cap on resale should be modified or eliminated and whether the transmission services described in the NOPR are suitable for reassignment.

---

[309]See Section IV.A.5.

[310]*FERC Statutes and Regulations* ¶32,514 at p. 33,088.

General

Many commenters favor capacity reassignment and the development of secondary markets.[311] However, WP&L notes that reassignments should not be permitted over constrained interfaces if the **[31,695]** source or destination of power changes, and LA DWP opposes unrestricted reassignment because it could cause tax-exempt financing problems for many public power utilities.

Many IOUs argue that the same terms and conditions of service applied to IOUs should be applied to resellers of transmission services?[312] Arizona Public Service. however, asserts that all unused transmission rights should not be assignable, but should be made available to others in a manner consistent with the contract supporting the rights, it argues that a network user experiencing an off-system network shutdown should be required during the outage to make available to others the path from the point that the power enters the system to its load. It also contends that firm transmission customers should be required to post their unused rights on an EBB or RIN.

Several commenters oppose mandatory reassignment of firm capacity rights.[313] NEPCO declares that if a customer

---

[311]*E.g.*, PacifiCorp, DOJ, NIEP, ELCON. United Illuminating, DOD, WP&L, FTC, OK Com and FL Com favor reassignment of capacity that reliability not be affected.

[312]*E.g.*, Northern States Power.

[313]*E.g.*, NEPCO, Nebraska Public Power District.

is willing to pay for its reserved capacity, it should not be forced to reassign unused capacity. Nebraska Public Power District believes that mandatory reassignment could cause problems for publicly-owned utilities. It further asserts that in the gas industry the Commission did not allow the unregulated reassignment regime it proposes for the electric industry.

SoCal Edison argues that when a transmission customer resells transmission capacity, it should not be released from its contractual obligation to the transmission provider. It notes that under traditional contract law, a party to a contract cannot escape its obligations by delegating them to another.

Price Caps

Most commenters addressing this issue support retaining the existing price capon reassignments or resales.[314] Generally, these commenters believe that the price cap is necessary to prevent customers from speculating or hoarding capacity in anticipation of its value increasing. Public Service Co of CO believes that allowing assignments of capacity at prices greater than cost could prevent a transmission provider from offering firm capacity for legitimate long-term transactions. TDU Systems states that a cap should remain

[314]*E.g.*, NRECA, Montana Power, PacifiCorp. NYSEG, PA Corn, Idaho. Public Service Co of CO, FPC, Entergny, TDU Systems, Duke, Cajun, CVPSC, Oglethorpe, Minnesota DPS. FL Com argues that the price of reassignment should be capped at the contract selling price. WP&L argues that the price cap should be raised to the maximum rate allowed in the tariff under which the user purchased the original service.

until the secondary market in the relevant geographic market has been shown to be competitive. PA Corn states that turning available capacity into a spot market would tie up capacity that might otherwise be used on a day-to-day basis and for emergencies. Still other commenters argue that customers should not be allowed to sell the capacity for more than the transmitting utility could charge.[315] Allegheny argues that any rule that allows resale of transmission capacity at a higher price than the transmission provider can achieve is "patently illogical and probably illegal." Several utilities, including Allegheny and CSW. contend that if resellers can market transmission services at market rates, then transmission owners must be given the same opportunity.

Duquesne and United Illuminating argue that the price cap should be modified so that third parties are allowed to resell capacity at the higher of embedded costs or opportunity costs.[316] Duquesne notes that such a provision would be comparable to the option transmitting utilities now have and would be economically effi-dent because it would encourage the firm capacity owner with the lowest opportunity cost to resell its capacity.

[31,696]

A few commenters argue that the price cap should be eliminated.[317] IL Corn claims that capacity will be made available to the entity that values it most and that an uncapped

[315]See also Minnesota DPS.

[316]See also Midwest Commission, SMUD, CCEM.

[317]*E.g.*, IL Com, NEPCO, Consumers, American Wind.

resale market cannot lead to more market power because an efficient secondary market cannot be monopolized. Con Ed agrees that if the secondary market is competitive, all entities should be allowed to sell at market-based rates.[318] CT DPUC argues that there should not be a price cap: instead, it would prefer that those holding transmission rights not be allowed to withhold use of any portion of their reserved transmission capacity in the actual moment-by-moment operation of the grid.

Creditworthiness Standards

Of those commenting on the appropriate creditworthiness standards for replacement customers (assignees), all favor allowing the transmission provider to use reasonable credit procedures to assure that the replacement customer is financially sound.[319] NYSEG suggests that. at a minimum, the same creditworthiness criteria should be applied to the replacement customer as are applied to the original customer. Oglethorpe recommends that the assignee be required to commit to comply with all customer obligations and to pay for any additional costs resulting from the assignment.

Liability for Payment

Commenters split on whether the original customer or the replacement customer should be liable to the transmitting

---

[318]If the market is not competitive, however, Con Ed maintains that the cap should be retained for all entities.

[319]*E.g.*, PacifiCorp, NYSEG, Oglethorpe.

utility for payment for the service. One group of commenters believes that the original customer should remain liable for all costs and for the performance of all obligations.[320] Another group of commenters believes that the original customer should be relieved of financial responsibility, at least under certain circumstances.[321] For example. NYSEG asserts that the original customer should be relieved of its obligations upon the execution of a new service agreement between the new customer and the provider. TDU Systems contends that the original customer should be relieved of future liability where the replacement customer meets the transmission provider's creditworthiness standards. Entergy argues that the original customer should, remain liable until all obligations are fulfilled.

Commission Conclusion

After reviewing the comments, we conclude that a. public utility's tariff must explicitly permit the voluntary reassignment of all or part of a holder's firm transmission

---

[320]*E.g.*, Oglethorpe, NSP.

[321]*E.g.*, NYSEG, Entergy, TDU Systems, Trulock, American Wind.

capacity rights[322] to any eligible customer.[323] Reassignment may be on a temporary or permanent basis, and must be subject to the condition and requirements discussed below.

Allowing holders of firm transmission capacity rights to reassign capacity will: (1) Help them manage the financial risks associated with their long-term transmission commitments, (2) reduce the market power of transmission providers by enabling customers to compete, and (3) foster efficient capacity allocation. We offer below a number of clarifications and further explanations in response to concerns raised by commenters.

(1) Reassignable Transmission Services

We conclude that point-to-point transmission service, because it sets forth clearly defined capacity rights, should be reassignable. As for network transmission service, we conclude that there are no specific capacity rights associated with such service, and thus. network transmission service is not reassignable.

---

[322]The transmission provider has the same rights as any other potential assignee to obtain capacity that is posted on an OASIS or to negotiate with the assignor for any capacity the assignor seeks to assign.

[323]The public utility's tariff shall not preclude an assignor from including a right of recall in its agreement with an assignee.

(2) Terms and Conditions of Reassignments

a. General

In effecting a reassignment, the assignor does not have to return its capacity entitlement to the original transmission **[31,697]** provider, but may deal directly with an assignee without involvement of the transmission provider. However, an assignee must meet the eligibility standard established by this Rule and must comply with the reliability criteria of the original transmission provider. Any such transaction must be posted on the transmission provider's OASIS within a reasonable time after its effective date. Alternatively, the assignor may, if it wishes, request the transmission provider to effect a reassignment on its behalf.[324] In such a situation, the transmission provider must immediately post the available capacity on its OASIS. The transmission provider must assure that any revenues associated with the reassignment are credited to the assignor.[325]

---

[324]The assignor may also request the transmission provider to provide the billing and payment services for the reassignment. The parties would negotiate terms for such an arrangement, including a fee for the transmission provider. If an assignor is a public utility, it will have to have on file with the Commission a rate schedule governing reassigned capacity.

[325]Any expenses that the public utility incurs in carrying out the capacity assignment program would simply be included in its cost of service.

b. Contractual Obligations

Assignors and assignees may contract directly with each other, but the assignor will remain obligated to the transmission provider, This obligation extends to any penalties or other charges incurred by the assignee in its use of the reassigned capacity, The assignee will be liable solely to the assignor, and should it not meet its obligations, the assignor may cancel the assignment under their contract.

If the transmission provider and the original customer mutually agree, we will permit alternatives to the above approach. For example, the transmission provider could agree to relieve the original customer of payment liability for the term of the reassignment and permit the assignee to pay the provider directly.

In the case of a permanent reassignment. the transmission provider should not unreasonably refuse to release the assignor from liability if the assignee meets the transmission provider's creditworthiness requirements as set forth in its tariff and agrees to pay the price the assignor is obligated to pay the transmission provider.

c. Price Cap

We conclude that the rate for any capacity reassignment must be capped by the highest of: (1) The original transmission rate charged to the purchaser signor), (2) the transmission provider's maximum stated firm transmission rate in effect at the time of the reassignment, or (3) the assignor's own opportunity costs capped at the cost of expansion (Price Cap). We remain convinced that we cannot

lift the Price Cap and permit reassignments at market-based rates. Based upon the information available in this proceeding, we are unable to determine that the market for reassigned capacity is sufficiently competitive so that assignors will not be able to exert market power. Thus, we will not permit an assignor to reassign capacity at a rate in excess of the Price Cap. Assignees must agree, in contracting with the assignor, that the firm transmission capacity they will use is subject to the Price Cap.

7. Information Provided to Transmission Customers Comments

Many commenters argue that in an open access, competitive environment, confidential and proprietary information should not be made publicly available through a RIN.[326]

Several utilities assert that the existing reporting requirements are sufficient to support the comparability requirements of the proposed rule, with some modifications.[327] They note that the Commission's audit authority and complaint process will help enforce comparability requirements.[328] Central Illinois Public Service

---

[326]Similar arguments with respect to the information that public utility must provide to the Commission in standard reports (*e.g.*, Form No. 1) are addressed later in this Final Rule.

[327]*E.g.*, PacifiCorp, NYSEG, NSP.

[328]See also PA Com.

states that, with the availability of pricing and transaction information through the RIN, no further reporting requirements are necessary. IL Com states that additional reporting should be required only if clear evidence emerges of discriminatory use of the transmission system. Dominion Resources adds that users have **[31,698]** no need for utility planning information and data on generator status and that disclosure of such information would place owners at a competitive disadvantage. VEPCO opposes the disclosure of any commercially sensitive information to marketers, including the utility's power marketing employees.

On the other hand, several commenters argue that the information submitted by public utilities may not be adequate. For example, APPA argues that the Commission should scrutinize closely cost functionalization by utilities to assure that plant in service is properly booked. Others recommend that the Commission put in place a monthly pass-through of transmission-related operating income for all classes of customers receiving firm transmission service, rather than rely on the current practice of reducing test year cost of service by revenues booked to Accounts 456 and 447. Industrial Energy Applications recommends that utilities be required to file quarterly reports with the Commission that detail the transmission services and the pricing of their off-system power supply transactions, as an incentive to comply with the Commission's rule. Commission Conclusion

We conclude that all necessary transmission information, as detailed in the OASIS final rule, must be posted on an OASIS. With respect to generation information, we will require, consistent with the OASIS final rule, that information needed to verify opportunity/redispatch costs be

provided, on request, to the transmission customer charged, We will not require this information, or any other generation information,[329] to be posted on an OASIS.[330]

[31,698]

8. Consequences of Functional Unbundling

a. Distribution Function

The NOPR proposed functional unbundling of wholesale generation and wholesale transmission so that the public utility as a wholesale seller could not gain an undue advantage from its transmission ownership. We did not propose to further unbundle the retail transmission and distribution functions from the wholesale transmission function.

---

[329]The prices of some ancillary services, which are posted on the OASIS, are based on generation tusks, however.

[330]Because the Commission establishes many generation and all transmission rates on a cost basis, the Commission also will continue to sell the information that it collects in Form No. 1 and other standard forms from public utilities to assure that the rates arc just and reasonable. As we explain later in this Final Rule. the information provided in those forms is public information that is available to any transmission customer. However, because of the competitive changes occurring in the electric industry, we recognize that there may be a need to reexamine the information we collect from public utilities through the Form No. 1.

Comments

A number of commenters assert that utilities should be required to unbundle -- either functionally or corporately -- the distribution function from the transmission function. ELCON argues that unbundling distribution would help delineate state and Federal jurisdiction, facilitate the establishment of transmission pricing, avoid cross-subsidization, and prepare for the customer choice (retail wheeling) programs that will be implemented by states in the future. It contends that functional distinctions between wholesale and retail service should be minimized.[331]

Other commenters, however, oppose establishing a separate distribution function. DOD asserts that the Commission can address any problems that arise by enforcing the terms of open access tariffs and that the Commission should not intrude into state ratemaking.[332]

Various state commissions question the workability and desirability of a functional test to determine the dividing line between retail transmission and local distribution.[333] CA Com recommends that, to avoid jurisdictional uncertainty surrounding functional unbundling, the Commission adopt a functional test for local distribution. Under this test, vertically

---

[331]See also Environmental Action, Missouri Basin MPA, Texaco, EGA, AEC & SMEPA.

[332]See also TDU Systems, Public Service Co. of CO.

[333]*E.g.*, NARUC, AZ Com, CT DPUC, OK Com, FL Com, NC Com, NM Com.

integrated utilities that chose to unbundle **[31,699]** into separate operating companies, including a local distribution company that sells only at retail, could establish a workable bright line between state and federal authority without engaging in the arduous task of differentiating transmission from distribution.

Certain IOUs echo the jurisdictional concerns raised by the state commissions.[334] They believe that the unbundling of the distribution function would create significant jurisdictional problems. Pacificorp also argues that unbundling of the distribution function would create significant jurisdictional conflict with respect to cost allocation.

Commission Conclusion

We conclude that the additional step of functionally unbundling the distribution function from the transmission function is not necessary at this time to ensure non-discriminatory open access transmission. Our approach to assuring such open access has two broad requirements: (1) functional unbundling of transmission and generation (which includes separately stated rates for generation, transmission, and ancillary services, and a requirement that a transmission provider take service under its own tariff), except for bundled retail service and (2) an OASIS with standards of conduct. We believe that additional requirements are not needed now. We further address in Section IV.I the concerns raised regarding

---

[334]*E.g.*, Com Ed, Citizens Utilities, PacifiCorp.

our proposed tests to distinguish transmission and local distribution.

b. Retail Transmission Service

The majority of commenters addressing this issue believe that unbundling retail service is unnecessary to establish a competitive market and to achieve non-discriminatory open access transmission.[335] For example, PSNM argues that the Commission is not as well situated as are state regulators to oversee and supervise local reliability issues for retail customers. Central Illinois Public Service argues that due to the nature of transmission facilities and operations, it is not possible for the transmission provider to discriminate between the provision of wholesale and retail firm service. Several IOUs further contend that because the Commission is specifically precluded from mandating retail wheeling and has no authority over bundled retail service, the Commission cannot require retail service to be provided.[336]

In contrast, some commenters argue that functional unbundling must apply to all transmission service in interstate commerce provided by public utilities, including the transmission component of bundled retail sales.[337] They believe that this is necessary to achieve comparability. For

---

[335]*E.g.* Allegheny Power, PacifiCorp, MidAmerican, PECO, Public Service Co of CO, Com Ed, NARUC, NRRI, MN DPS, ND Com, FL Com.

[336]*E.g.*, Allegheny Power.

[337]*E.g.*, CCEM, ABATE.

example, CCEM asserts that if the distribution function is not unbundled, the result will be service under two separate arrangements -- an explicit wholesale transmission tariff filed at the Commission and an implicit retail transmission tariff governed by a state regulatory body. According to CCEM, failure to unbundle retail transmission will allow transmitting utilities to manipulate how they characterize and account for their own uses of transmission. ABATE contends that the Commission, for efficiency reasons, should encourage states to permit retail access. It asserts that the Commission must adopt a policy that signals to states how rates, terms, and conditions of retail service will be established; once a state sets such parameters, the Commission should review them.

Commission Conclusion

Although the unbundling of retail transmission and generation, as well as wholesale transmission and generation, would be helpful in achieving comparability, we do not believe it is necessary. In addition, it raises numerous difficult jurisdictional issues that we believe are more appropriately considered when the Commission reviews unbundled retail transmission tariffs that may come before us in the context of a state retail wheeling program. The Commission therefore reaffirms its decision to require the unbundling **[31,700]** only of wholesale transmission from generation.[338]

---

[338]But see discussion of buy/sell transactions in Section IV.I.

c. Transmission Provider

1. Taking Service Under the Tariff

In the NOPR, we explained that a public utility must take transmission services for all of its new wholesale sales and purchases of energy under the same tariff of general applicability under which others take service.[339]

A number of commenters argue that utilities should be required to take all of the transmission for their own use under their tariff.[340] CCEM asserts that a transmission owner should have to schedule, at arm's length, its retail transmission uses and pay posted rates into a separate account; otherwise the capacity might be overforecast at no cost.

PECO requests that the Commission clarify that the requirement that a transmission provider take service under its own transmission tariffs does not apply to: (1) retail service, (2) existing wholesale contracts, and (3) pooling arrangements. UNITIL claims that the requirement for a transmission provider to take service under its own tariff and to post its own tariff rate should not apply to pool transactions where a single pool-wide rate is applied.

A number of IOUs contend that it is not necessary for the transmission provider to take service under the network

---

[339]*FERC Statutes and Regulations* ¶32,514 at p. 33,080.

[340]*E.g.*, Michigan Systems, Cleveland, Municipal Energy Agency Nebraska, Missouri Basin MPA, TAPS, Wisconsin Municipals, LG&E, NIEP, CCEM.

tariff because both the transmission provider and the network customers cannot use the tariff to make off-system sales. LILCO states that it is appropriate to distinguish between a transmission owner's use of its transmission system to make: (1) wholesale bulk power sales; and (2) off-system purchases to serve its native load retail customers. LILCO contends that in the second situation it should not be required to take transmission service under its own open access tariffs.

EGA argues that transmission owners should be required to take transmission service under open access tariffs for both wholesale off-system sales and purchases. It maintains that, as retail competition increases, utilities will eventually have to take retail service under their own tariffs. Power Marketing Association believes that comparability can be achieved only if transmission service provided in connection with coordination transactions is unbundled and the transmission provider takes such transmission service under its tariff.

Consumers Power also claims that there is an inconsistency between the NOPR text, the tariffs, and the proposed regulatory language regarding whether the requirement for a utility to take service under its own tariff applies only to new wholesale transactions. Commission Conclusion

We conclude that public utilities must take all transmission services for wholesale sales under new requirements contracts and new coordination contracts under

the same tariff used by others (eligible customers).[341] For sales and purchases under existing bilateral economy energy coordination agreements, we will give an extension until December 31, 1996, for public utilities to take transmission service under the same tariff used by others.[342] As further discussed in Section IV.F., we will also give an extension of time to December 31, 1996, for certain existing power pooling and other multi-lateral coordination agreements to comply with this requirement. This will ensure that utilities live by their own rules for wholesale transactions and that we can achieve non-discriminatory open access transmission. In the case of a public utility buying or selling at wholesale, the **[31,701]** public utility must take service under the same tariff under which other wholesale sellers and buyers take service.

2. Accounting Treatment

In the NOPR, we did not address any accounting aspects of our proposed rule.

---

[341]With the exception of certain contracts and agreements executed on or before 60 days after publication of the Final Rule in the Federal Register, the regulation we are adopting requires that public utilities take service under their open access tariff for wholesale sales or purchases of electric energy and unbundled retail sales of electric energy, effective on the date the public utility engages in such transactions.

[342]As discussed in Section IV.F., the Commission will not impose this requirement on existing bilateral non-economy coordination agreements, but persons may file complaints that such agreements need to be modified.

IOUs generally object to a requirement that they pay themselves for their use of the transmission system.[343] NEPCO claims that it is a general principle of accounting that an enterprise cannot recognize and record revenues to itself. NEPCO suggests that, to ensure that utilities' financial statements are not misleading, this aspect of functional unbundling can and should be accomplished through the ratemaking process, rather than by requiring utilities to actually charge themselves revenues for taking transmission services.[344]

Atlantic City Electric states that the added costs of properly administering and accounting for these transactions separately will increase prices to ultimate consumers. It contends that ensuring that operators do not give undue preference to transactions of the transmission provider makes it unnecessary for a utility to charge itself.

CSW argues that some of the provisions of the tariffs were specifically designed for third parties and do not make sense as applied to the transmission provider (e.g., signing service agreements and running credit checks).[345]

Most IOUs suggest that a revenue credit mechanism be used to account for a transmission provider's use of its system. Florida Power Corp states that revenue credits should be equal to the utility's posted rates for transmission service

---

[343]*E.g.*, EEI, Con Ed, VEPCO.

[344]See also NEPCO.

[345]See also Florida Power Corp.

multiplied by the amount of capacity reserved and/or energy transmitted by the utility.

Otter Tail proposes a revenue credit that allocates revenues based on use under the tariff of the utility's transmission investment and credits these revenues against the firm load customers' accounts.

Duke asserts that the transmission provider should maintain records reflecting transmission for its own transactions under the tariff and develop appropriate revenue credits for transmission rates. It also believes that all firm users of the transmission system should receive credits for all non-firm uses.

Allegheny Power states that the crediting of non-firm revenues to network customers would have to be done on an after-the-fact basis when their loads would be known. However, it believes that revenue crediting should occur only if the firm service customer has retained the utility to remarket the customer's unused capacity.

Cajun proposes that all transmission revenues in excess of those implicitly included in the development of the transmission rates, including those that the utility has charged itself, be credited back to the network service transmission customers on a load ratio share basis. If transmission service rates are formula rates that are recalculated annually, Cajun proposes that excess transmission revenues be used to offset the recalculated revenue requirement. If the rates are not formula rates, Cajun states that an explicit tracker with monthly crediting to the network customer must be used.

To avoid cross-subsidization between affiliates and third parties, NRECA suggests that transmission revenues "paid" by a utility's generation function to its transmission function be credited back to the utility's nonaffiliated customers, and that any rate discounts extended to the generation function by the transmission function be filed with the Commission with a full explanation of why the discount was extended together with a showing that the discount was made available to all other similarly situated customers.

APPA contends that the Commission's current system of revenue crediting could give transmission owners an unfair competitive advantage by allowing them to use the revenue credit to subsidize the price at which they sell power. It argues that transmission owners should pay the actual price of transmission rather than booking a revenue credit as an offset to the cost of transmission service.

TAPS and Wisconsin Municipals argue that an essential element of true comparability **[31,702]** is the ongoing pass-through to network customers of a load ratio share of transmission revenues generated by third-party and the transmission provider's off-system uses of the transmission system.

Houston L&P suggests that the revenue crediting mechanism proposed in the NOPR could be established to recognize the utility's transmission service revenue and expenses in non-third-party wheeling transactions by reclassifying a portion of its revenue equal to the cost of transmission services provided to itself during such transactions. This mechanism would not reclassify expense accounts, but would distinguish that transmission portion of

the total transaction's revenue that was associated with covering the cost of transmission service, using the rates charged in similar third-party transactions.

PacifiCorp contends that the Commission should enforce the requirement that utilities account for revenues they pay themselves through the Commission's audit powers and through complaint proceedings. It specifically recommends that each transmitting utility be required to indicate, in its Form No. 1 under Account 456, the megawatts and revenues associated with its firm and non-firm off-system sales.[346]

MT Com states that the embedded costs that the Commission functionalizes for jurisdictional purposes should be carefully reconciled with plant balances used to calculate other costs of service.

CCEM wants each transmission provider to charge and book revenues into separate accounts for (1) service provided to itself and off-system sales and third-party sales under the tariffs, (2) impact study costs that the provider performs for itself or an affiliate, and (3) ancillary service revenues, net of out-of-pocket expenses the transmission owner provides itself or an affiliate.

Arizona Public Service recommends that any revenue crediting or booking be prospective only and that enforcement

---

[346]If the utility is not required to file a Form No. 1, PacifiCorp states that it should be required to file similar information annually.

occur through the Commission's periodic audits and a utility's rate cases.

Many IOUs argue that there should be no obligation to credit non-firm transmission revenues to customers who are not using their firm capacity.[347] PacifiCorp contends that all non-firm revenues should be credited against total annual revenue requirements, resulting in lower rates to all customers. Wisconsin P&L maintains that non-firm sales revenue should be shared with all network customers.

Otter Tail argues that non-firm transactions between existing utilities to support and achieve real-time system optimization should be permitted without charge to the transmission owner. CSW asserts that no credits should be made for the non-firm secondary service under the point-to-point tariff and that off-system purchases for native load should not result in a revenue credit.

Southwestern suggests that the Commission not require the crediting of a transmission component associated with off-system purchases by the public utility. Southwestern argues that a credit would interfere with a utility's ability to buy the most economic energy for its native load customers. It also argues that requiring a credit is not comparable to what network customers pay. NEPCO points out that crediting transmission associated with purchases would require native load customers to pay the costs of the utility's purchasing off-system power while network customers do not have to pay a

---

[347]*E.g.*, Consumers Power, Northern States Power, PacifiCorp, Allegheny Power.

separate point-to-point charge for their off-system purchases. Southwestern claims that the crediting requirement would double-charge the transmitting utility and its native load customers because a utility's off- system purchases directly relate to the load it serves, and that load already is reflected in the transmission rate calculation. Southwestern also claims that it is unclear from the NOPR whether the Commission considers sales from the renewal of existing wholesale requirements contracts as being subject to crediting. It argues that transmission related to these sales should not be subject to the crediting requirement because this is service to native load customers.

[31,703]

Brazos opposes imputing revenues associated with a utility's own use of its transmission system because this will artificially increase the cost of power and deny consumers the benefits of economy energy sales made at market-based prices. Commission Conclusion

While we used the word "accounting" in the NOPR, the real issue is assuring that utilities bear the costs associated with their own uses of the system in a manner comparable to how they charge others. Accordingly, this is a rate issue, not an accounting issue. However, we direct utilities to account for all uses of the transmission system and to demonstrate that all customers (including the transmission provider's native load) bear the cost responsibility associated with their respective uses.[348]

---

[348]Additional guidance on this subject is in Section IV.G.4.g.(2)(a).

* * * * *

[pp. 31,718 - 31,736]

[31,718]

b. Services that May Be Offered and Sold as a Package

The NOPR indicated that ancillary services must be offered separately from one another but did not indicate if the transmission provider may also offer a package of ancillary services.

Comments

Several commenters support giving customers the option either to purchase ancillary services as separate and distinct services or to purchase a package of services from the transmission provider.[394] Others, such as Tallahassee, recommend that utilities be prohibited from bundling the purchase of one service with another so that a transmission customer cannot **[31,719]** rely on the transmission provider for just one or a few of the ancillary services.

EEI and ELCON argue that the Commission should permit customers the option to request that transmission providers offer packages of selected ancillary services.[395] They and other commenters express a concern that

---

[394]*E.g.*, Direct Service Industries, Mt. Hope Hydro, ELCON, PA Com.

[395]EEI Initial Comments at V-4; ELCON Initial Comments at p. 21.

efficiencies can be lost under a policy that precludes combining ancillary services.

Commission Conclusion

We conclude that a transmission provider must offer and price the individual ancillary services separately. It may not tie the purchase of one to the purchase of another.

However, we will allow a transmission provider to assemble packages of ancillary services (not bundled with basic transmission service) that can be offered at rates that are less than the total of individual charges for the services if purchased separately. It may also offer rate discounts on any ancillary service. If a rate discount is offered to the transmission owner itself or to an affiliate of the transmission owner, the same discount must be offered to non-affiliates, as well. In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory. All discounts must be posted on the transmission provider's OASIS.

4. Reassignment of Ancillary Services

In the NOPR, the Commission noted that ancillary services may not be suitable for reassignment and requested comments on this issue.

Commenters express divided views on the reassignment issue. Some IOU commenters believe that, subject to technical limitations, ancillary services could be

reassigned.[396] Other commenters, including many IOUs, oppose reassignment because they believe it is impractical.[397] In particular, PacifiCorp claims that the customer-specific nature of generation-related ancillary services prevents such services from being reassigned.

TDU Systems argue that transmission customers that must pay for ancillary services they do not need should be able to resell them to someone else.[398] Mt. Hope Hydro claims that, if a bulk power transaction and the associated transmission service can be reassigned, it is reasonable that the ancillary services used to support the transaction also should be reassigned, particularly if the same facilities and contract path are used.[399]

Commission Conclusion

We conclude that transmission customers will be allowed to reassign ancillary services along with the reassignment of basic transmission service. The Commission believes that a policy of transmission capacity reassignment may not be possible unless the ancillary services used to support the transmission are also reassignable.

---

[396] *E.g.*, WP&L, NYSEG.

[397] *E.g.*, Consumers, PacifiCorp, Carolina P&L, PSNM, Salt River, PA Com, TDU Systems.

[398] TDU Systems Initial Comments at p. 87.

[399] Mt. Hope Hydro Initial Comments at p. 17.

5. Pricing of Ancillary Services

In the NOPR, we asked for comments on ancillary service pricing and proposed specific ancillary services prices in the Stage One implementation rates. Many commenters commented on the Stage One rates. There is no Stage One in the Final Rule.

Many commenters state that ancillary services are difficult to price. They suggest diverse pricing approaches. IN Com notes that, because utilities and regulatory commissions have no experience with pricing unbundled ancillary services, the process needs to evolve but the goal should be to encourage market pricing in competitive markets. Air Liquide believes the best pricing policy should be negotiated bilateral agreements, provided market power is mitigated.

Other commenters express concern about how pricing proposed in the NOPR would affect the development and operation of competitive ancillary services markets. Industrial Energy Applications notes that low price caps on generation-related services, such as supplying losses, imbalance energy, operating reserve and backup power, which can be provided from many sources, inhibit competitive **[31,720]** market development. There is little incentive for other providers to invest in facilities to provide these services. Dayton P&L and others contend that the Commission should not require transmission providers to provide generation-based ancillary services at cost-based rates and then allow third parties to resell such services at market-based rates. PacifiCorp expresses concern that the NOPR's pricing proposal would be overly restrictive in the emerging competitive market for generation-related ancillary services.

Many commenters argue that cost-based price caps are appropriate for ancillary services if there are no alternative suppliers or until competitive markets develop.[400] CAMU suggests that the comparability standard is not met if market rates exceed the costs of providing ancillary services. Allegheny, Ohio Edison and Atlantic City support cost-based pricing for Reactive Power/Voltage Control. Ohio Edison recommends cost-based pricing for frequency regulation, and Atlantic City recommends it for scheduling and dispatch.

Several commenters suggest that the Commission require cost-based rates for ancillary services where no source other than the transmission provider exists and market-based rates for generation-related ancillary services if competition exists.[401] Washington and Oregon Energy Offices recommend that, before permitting market-based rates, at least two other non- affiliated parties should be able to offer a nearly identical ancillary service and that the Commission should use the same standards for allowing market-based rates for ancillary services that it has used for wholesale power sales. Mt. Hope Hydro argues that vertically integrated utilities should be permitted to charge cost-based rates that are limited to no more than the market price for ancillary services. It also contends that companies whose generation facilities are not supported by captive retail or transmission customers should be authorized to sell at market-based prices.

---

[400] *E.g.*, Utilities For Improved Transition, Idaho, CINergy, Direct Service Industries, Mt. Hope Hydro, ABATE, TDU Systems, Missouri-Kansas Industrials, Washington and Oregon Energy Offices, IN Com.

[401] *E.g.*, PJM, Texas Utilities, Entergy, Carolina P&L.

The vast majority of commenters from all interest groups who address market-based pricing for ancillary services agree that market-based pricing is appropriate for ancillary services where competitive market conditions exist. However, commenters disagree over whether a competitive market for ancillary services currently exists.

In determining the extent of competition, many commenters distinguish between ancillary services that are (1) generation- related and (2) transmission-related. Commenters disagree over whether the Commission can declare generation-related ancillary services to be competitive on a generic basis. Many commenters contend that transmission-related ancillary services are not available in a competitive market; consequently, they agree that prices for such services should be cost-based.

Commission Conclusion

We will consider ancillary services rate proposals on a case-by-case basis.

In response to comments,[402] we offer here some general guidance on ancillary services pricing principles.

---

[402]Many commenters were particularly concerned that rates for energy losses, a NOPR ancillary service, should be market-based. We need not address this concern in this Rule, however, because we will not require Real Power Losses to be offered as an ancillary service.

(1) Ancillary service rates should be unbundled from the transmission provider's rates for basic transmission service, even though such services are a necessary adjunct to basic transmission service.

(2) The fact that we have authorized a utility to sell wholesale power at market-based rates does not mean we have authorized the utility to sell ancillary services at market-based rates.

(3) In the absence of a demonstration that the seller does not have market power in such services, rates for ancillary services should be cost-based and established as price caps, from which transmission providers may offer a discount to reflect cost variations or to match rates available from any third party. If a rate **[31, 721]** discount is offered to the transmission owner itself or to an affiliate of the transmission owner, the same discounted rate must be offered to non-affiliates, as well. In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory. All discounts must be posted on the transmission provider's OASIS.

(4) The amount of each ancillary service that the customer must purchase, self-supply, or otherwise procure must be readily determined from the transmission provider's tariff and comparable to the obligations to which the transmission provider itself is subject. The provider must take ancillary services for its own wholesale transmission under its own tariff.

(5) The location and characteristics of a customer's loads and generation resources may affect significantly the

level of ancillary service costs incurred by the transmission provider. Ancillary service rates and billing units should reflect these customer characteristics to the extent practicable.

6. Accounting for Ancillary Services Comments

Some commenters suggest that there may be a need for revising the Uniform System of Accounts to track better the costs of providing discrete ancillary services. Other commenters believe that ancillary services are transmission-type services and suggested that the costs of generation-provided ancillary services be refunctionalized from power production expense to transmission expense.

Oak Ridge asserts that a primary goal of those interested in restructuring the electricity industry should be to identify clearly the different functions that are today buried within the vertically integrated utility and bundled into one price. Oak Ridge, however, indicates that achieving this ideal of identifying unbundled services at appropriate prices will be difficult because of utility accounting practices.

EEI asserts that since the current Uniform System of Accounts was designed to track costs incurred to provide bundled wholesale service, it does not track the discrete costs incurred to provide ancillary services. Therefore, according to EEI, a major update is needed to support the pricing of discrete ancillary services.

ConEd states that ancillary services are integral and essential elements of providing transmission services. It notes that, historically, due to the vertical integration of utilities, those services have been bundled with the other services

provided and the costs associated with providing ancillary services have not been specifically defined. ConEd claims that to a large degree, this is due to the fact that utility accounting mechanisms were not established with the intention of identifying the costs for ancillary services.

UI asserts that if transmission customers are to be charged for certain ancillary services, it may be necessary to refunctionalize certain specific costs items from generation to transmission. UI points out that some of the reactive power to support system voltages and to provide transmission services, for example, is supplied from the variable reactive output of the generators. It states that these costs, to the extent they can be identified with the provision of transmission service, should be refunctionalized to the transmission account. However, UI states it may not be possible to develop a unit cost for specific transactions. Thus, UI states it may be more appropriate to roll these costs into the embedded transmission rate and allocate them among the various users of the transmission system.

Commission Conclusion

To ensure comparable transmission access a Transmission Provider is obligated to offer or arrange to provide certain ancillary services to the Transmission Customer. Also, the Transmission Provider may offer to provide other ancillary services to the Transmission Customer. A Transmission Customer is obligated to purchase certain ancillary services from the Transmission Provider.

Generation resources provide certain ancillary services, while transmission resources provide other ancillary

services. Consequently, the costs of providing certain ancillary services are recorded in the utility's power production expense accounts, while others are recorded in the utility's transmission expense accounts.

Currently, the Uniform System of Accounts requires that costs incurred in providing ancillary services be recorded as power production or transmission expense depending upon which resource the utility uses to supply the service. At this time, **[31,722]** we are not convinced that the amounts involved or the difficulty associated with measuring the cost of ancillary services warrants a departure from our present accounting requirements. We will specify, however, that revenues a Transmission Provider receives from providing ancillary services must be recorded by type of service in Account 447, Sales for Resale, or Account 456, Other Electric Revenues, as appropriate.

E. *Real-Time Information Networks*

In the Open Access NOPR, the Commission determined that in order to remedy undue discrimination, a utility must functionally unbundle its wholesale services, and that among the things required by functional unbundling is that the utility, when buying or selling power, rely upon the same electronic network that its transmission customers rely upon to obtain transmission information. Accordingly, the Commission accompanied its issuance of the Open Access NOPR with issuance of a notice of technical conference that initiated a proceeding in Docket No. RM95-9-000 to consider whether Real-Time Information Networks (RINS) or some other option would be the best means to ensure that potential customers of transmission services have access to the

information necessary to obtain open access transmission service on a non-discriminatory basis.[403]

The Commission affirms its conclusion that in order to remedy undue discrimination in the provision of transmission services it is necessary to have non-discriminatory access to transmission information, and that an electronic information system and standards of conduct are necessary to meet this objective. Therefore, we issue, in conjunction with this Final Rule, a final rule adding a new Part 37 that requires the creation of a basic OASIS and standards of conduct.[404]

The Phase I OASIS rules require each public utility (or its agent), as defined in section 201(e) of the Federal Power Act, 16 U.S.C. 824(e), that owns, controls, or operates facilities used for the transmission of electric energy in interstate commerce to develop and/or participate in an OASIS. The Phase I OASIS rules describe what information must be provided on the OASIS during Phase I and how OASIS must be implemented.

In addition, the new Part 37 contains a code of conduct applicable to all transmission providing public utilities. The code of conduct is designed to ensure that preferential access to information about wholesale transmission prices and

---

[403]See Real-Time Information Networks, Notice of Technical Conference and Request for Comments, 60 FR 17726 (April 7, 1995).

[404]In Phase II, we will continue to develop the requirements for fully functional OASIS. We expect to issue a final rule on Phase II OASIS requirements sometime in 1997.

availability is not available to employees of the public utility engaged in wholesale marketing functions or to employees of certain of the public utility's affiliates.

F. Coordination Arrangements: Power Pools, Public Utility Holding Companies, Bilateral Coordination Arrangements, and Independent System Operators Comments

Timing of Reformation

Many marketers, IPPs, and other nonmembers of pools request that the Commission immediately apply unbundling and transmission tariff requirements to all new transactions under existing pooling agreements. APPA states that the Commission should not deal with power pools as a "follow-on activity" because treatment of pools is an integral step in achieving transmission comparability. AEC contends that until pools publish open access tariffs, the Commission should permit applications for section 211 transmission orders from one or more applicants directed to multiple respondents.

Existing pools generally urge the Commission to allow time for the pools to propose alternative structures or agreements which would meet the objectives of the final rule. EEI states that the rule may create problems for power pools that will not be examined or understood by the Commission and the public until the Commission's pooling inquiry is completed; it requests that the pooling inquiry be completed before a final rule is issued. Duke recommends that implementation of open access transmission services by power pools be addressed in a separate proceeding because implementation **[31,723]** of open access for power pools raises complex issues.

EGA, among others, argues that new transactions under existing pooling agreements should not be grandfathered, but rather should be required to meet the functional unbundling requirements of the final rule. Some pool members argue that pool transactions are largely not wholesale transactions. For example, PECO (a member of PJM) requests the Commission to clarify that the delivery of pooled generation to pool members' native load is not a "wholesale purchase" of power and thus would not require taking transmission service under one's own open access transmission tariff. Another member of PJM, BG&E, interprets the proposed rule to require all PJM economy trades to be firm point-to-point services; it claims that such a requirement "jeopardizes the continued viability of the pool."

System-Wide Tariffs

Virtually all commenters on power pool issues state that the tariff requirements should not be applied directly to individual utilities who are members of "tight" power pools. ELCON, CCEM, and others argue that the pro forma tariff requirement should be applied directly to "tight" or "single system" power pools to avoid discriminatory "pancaking" of transmission rates. However, Duke argues that where there are both multiple owners and operators, as in "loose" pools, it is appropriate to have individual tariffs unless the pool members agree otherwise. DOE recommends a power pool file a single pool-wide tariff to offset problems associated with joint ownership or control of transmission. CT DPUC recommends that the Commission provide guidance for transmission access and pricing (so as to avoid needless disruption of present methods).

Flexible Treatment

Most commenters on power pools support recognizing regional differences among power pools and urge flexibility. PSE&G (a member of PJM) states that open access tariffs must be specially crafted to deal with power pool members. NYPP and PJM state that they are considering innovations and urge that their efforts not be stifled by any final rule. CSW proposes a region-wide pricing model based on power flows. NPPD, a member of the Mid-Continent Area Power Pool (MAPP), says MAPP is considering adopting the megawatt-mile approach to transmission pricing. SoCal Edison states that California utilities are developing a market-based power pool and that it is crucial for the final rule to be flexible to permit innovations throughout the country.

ELCON and power marketers, however, argue for uniformity and point out the difficulties of moving power from system to system where each system has varying standards or "pool rules." These commenters support uniform application of the terms and conditions in the pro forma tariffs to create a national standard.

NEPOOL emphasizes that since pools remain voluntary, the imposition of rules that are not acceptable to pool members simply increases the likelihood that members will withdraw and pools will disintegrate. For this reason, NEPOOL states that solutions to enhance competition (within a tight pool setting) are best identified through the consensus of pool members, which requires both time and flexibility on the part of the Commission.

DE, DC, NJ and MD Coms emphasizes its concern that a one-size-fits-all open-access policy, while perhaps benefiting subsets of individual suppliers and purchasers, may not be the best solution for the millions of retail customers who currently rely on power pools.[405] It wants the Commission to be aware that the individual commissions have begun a formal dialog among each other and with the PJM utilities to discuss possible regional solutions to transitional competitive issues.

Open Membership

NIEP and CCEM argue that the competitive playing field cannot be level unless nonmembers receive certain power pool services on terms comparable to those for pool members. Members of pools state that "return in kind" transactions are efficient, but that such transactions are not appropriate for those entities that **[31,724]** are not similarly situated to vertically integrated utilities.

EEI maintains that those seeking the benefits of pool membership must accept the burdens imposed on existing pool members (otherwise, they would have an advantage, not comparability). EEI believes that new pool participants can negotiate and "buy into" the pool resources. Many commenters claim that unbundling certain power pool services to accommodate open access will solve the problem.

---

[405] *E.g.*, DE Com, DC Com, NJ Com, MD Com.

MidAmerican states that if the Commission grants nonmembers access to pool transmission service, the Commission should allow a period of at least four years for pools to restructure and refile rate schedules to avoid the inequitable results which the Commission's requirements will impose on pool members.

MidAmerican contends that the Commission should authorize pool members to unilaterally withdraw from their pools if any restructuring or revision of rate schedules is unacceptable to the member. Holding companies

Allegheny, Southern, and other holding companies argue that coordination agreements among subsidiaries of a utility holding company system do not constitute a power pool and should not be subject to any obligations the Commission may place on power pools. Bilateral Coordination Agreements

Ohio Edison requests clarification that the Commission is not requiring new wholesale coordination transactions to be under the open access tariffs; they may be continued under existing coordination agreements. It stresses the importance of such agreements in making economy and emergency transactions.

A number of commenters agree that existing coordination contracts should not be abrogated or modified, and that transactions under these existing contracts should not be governed by the provisions of the pro forma tariffs.[406]

---

[406]*E.g.*, Central Louisiana, Dayton P&L, LPPC, MEAG, Missouri Basin Group, Montana-Dakota Utilities, Nebraska Public

These commenters generally argue that existing coordination agreements should not be abrogated or amended by the final rule because: (1) they were not negotiated in the environment envisioned by the NOPR; (2) coordination sales are beneficial to consumers and ratepayers (and thus it would not be in the public interest to curtail them); and (3) the termination of coordination agreements, which in some cases have been in place for years and are tailored to parties' peculiar circumstances, could cause severe hardships in certain regions (especially with regard to scheduling and curtailment).

PSNM contends that such agreements are the result of mutually beneficial bargaining. LPPC and MEAG argue that current contracts negotiated among parties provide cost savings to consumers, which may be foregone if existing contracts are modified. Central Louisiana suggests that the pro forma tariff provisions should be flexible enough to achieve comparability if applied to both existing and new coordination agreements.

Some commenters argue that there may be cases where it is inappropriate to modify existing coordination agreements to satisfy the requirements of the rule. They assert that coordination agreements providing for emergency transactions,[407] reliability,[408] and resource efficiency gains[409]

Power District, Ohio Edison, PSNM.

[407]*E.g.*, Arizona, Ohio Edison.

[408]*E.g.*, Soyland, NRECA.

[409]*E.g.*, APPA.

need special attention. However, Soyland believes that existing agreements need to be reviewed if there is substantial increase in wholesale power market transactions, at the customer's option. TDU Systems argues that coordination contracts supporting system reliability should be honored and given scheduling and curtailment preference. TDU Systems contends that any amendments should be at the parties' discretion rather than by Commission mandate.

Several commenters suggest that the proposed rule is unclear about whether only existing transactions under agreements already approved by the Commission will be exempt from functional unbundling, or whether the proposed rule also would exempt (or grandfather) new transactions entered into pursuant to existing approved contracts.[410] Other commenters recommend that the Commission **[31,725]** clarify that its policy on unbundling applies to all new transactions, whether pursuant to new or existing agreements.[411] ConEd and KCPL request clarification that purchases made to satisfy retail service are not subject to the requirements of the pro forma tariffs.

CCEM argues that all coordination transactions, including new transactions under existing agreements, should be unbundled to ensure that transmission providers are implementing the posted transmission rate. CINergy contends that the comparability standard should be applied to existing coordination agreements, including buy-resell agreements, to

---

[410]*E.g.*, APPA, CCEM, EGA.

[411]*E.g.*, APPA, CCEM, LG&E, EGA.

mitigate any unfair bulk power market advantages. Functional unbundling would ensure that a utility includes an EBB-posted transmission rate in the transaction charge. CINergy and Power Marketing Association recommend that the Commission use its authority under section 206 to require all utilities to file amendments to their existing coordination agreements providing for transmission service to be taken pursuant to the parties' open access transmission tariffs. Power Marketing Association further recommends that the Commission establish expedited procedures to address the situation arising from conflicting pro forma tariffs and existing coordination provisions.

Tallahassee also believes that the comparability standard should be applied to existing coordination agreements, but Tallahassee recommends that the Commission establish a transition period to allow for renegotiation among parties rather than imposing modifications to existing agreements. Renegotiation would provide an opportunity to retain previously bargained-for benefits. Detroit Edison also contends that many of the existing coordination agreements do not provide for the services required under the pro forma tariffs. Like Tallahassee, Detroit Edison recommends that the Commission allow sufficient time for parties to renegotiate existing agreements. CINergy suggests a three- year transition period.

Coordination Pricing Practices

EEI and PJM disagree with the Commission's assertion that current coordination pricing is no longer just and reasonable in the absence of an open access tariff. Ohio Edison and PA Com question the basis of the Commission's

preliminary conclusion that current coordination pricing is no longer justified in the absence of a seller's tariff offer of non-discriminatory open access transmission services. PA Com asserts that the Commission's underlying assumption of general lack of transmission access by wholesale customers has not been established as fact in the proposed rule.

MN DPS supports current coordination pricing methods provided that utilities have executed open-access tariffs. Missouri Basin Group argues that, if increased market competition materializes through open access, utilities will decreasingly rely on current coordination pricing if it no longer produces the most beneficial outcome. Missouri Basin Group recommends the Commission simply allow utilities to choose a pricing method even if a utility opts for a less beneficial outcome. Nebraska Public Power District also urges the Commission to avoid mandating coordination pricing methods. Nebraska Public Power District is concerned that this may impede establishing RTGs where such pricing is by mutual agreement and subject to ADR procedures.

Several commenters agree that current coordination pricing may no longer be appropriate in an open access regime.[412] FL Com believes that current coordination pricing should be replaced by market-based rates if open access transmission service is imposed by the Commission.

---

[412]*E.g.*, Arizona, CINergy, Consumers Power, EEI, PJM.

Commission Conclusion

The term "coordination" is applied to a wide variety of wholesale power sales agreements within the industry, including interchange, interconnection, pooling, and other agreements. Broadly speaking, any non-requirements power sales agreement can be considered to be a coordination agreement.[413]

The Final Rule's general requirement for non-discriminatory transmission access **[31,726]** and pricing by public utilities, and its specific requirement that public utilities unbundle their transmission rates and take transmission service under their own tariffs, apply to all public utilities' wholesale sales and purchases of electric energy, including coordination transactions. The Commission has determined that certain existing wholesale coordination arrangements and agreements must be modified to ensure that necessary transmission services for such arrangements and agreements are taken under open access transmission tariffs and thus that such arrangements and agreements are not unduly discriminatory. Below we discuss how and when various types of coordination agreements will need to be modified, and when public utility parties to coordination agreements must begin to trade power under those agreements using transmission service obtained under the same open access transmission tariff available to non-parties.

---

[413]For example, a 30-year contract to supply 50 MW of power can be considered to be a coordination arrangement because it is not a contract to meet all of the buyer's power requirements.

Coordination arrangements, and the agreements governing them, vary widely. They range from relatively simple bilateral arrangements to complex tight power pools. Our discussion addresses four broad categories of arrangements and accompanying agreements: "tight" power pools, "loose" power pools, public utility holding company arrangements, and bilateral coordination arrangements. For purposes of implementing the non- discriminatory, open access requirements of the Final Rule, we are dividing bilateral coordination agreements into two general categories: bilateral economy energy agreements and other bilateral coordination agreements. Economy energy agreements typically provide for short-term economy trading "if, as, and when available" and are generally driven by the buyer and seller's generation costs. They do not require either the seller or the buyer to engage in a particular transaction. Other coordination agreements are typically longer term or open-ended. Some may involve joint ownership or joint planning of generation.[414] Others may provide joint operation of facilities so that the parties can coordinate their maintenance schedules or provide one another with emergency service. These longer-term coordination agreements are distinguished from short-term economy trading agreements in that the parties have undertaken a contractual obligation to operate their facilities so as to support one another under the conditions specified in the arrangements.

As noted in the NOPR, power pools, in contrast to most bilateral arrangements, present complex issues that may

[414]Agreements dealing with joint ownership or operation of transmission facilities are discussed at Section IV.C.3.

require special implementation requirements.[415] This is because these arrangements may involve agreements containing an intricate set of rights, obligations, and considerations among the members of a pool. We provide for implementation requirements herein that vary depending upon the type of "pooling" arrangement involved.

The Commission has concluded that in order to adequately remedy the undue discrimination in transmission access and pricing by public utilities that are members of power pools or other coordination arrangements, such public utilities must remove preferential transmission access and pricing provisions from agreements governing their transactions. The filing of open access tariffs by the public utility members of a power pool is not enough to cure undue discrimination in transmission if those public utilities can continue to trade with a selective group within a power pool that discriminatorily excludes others from becoming a member and that provides preferential intra-pool transmission rights and rates. The same holds true of certain bilateral arrangements that allow preferential transmission pricing or access. These arrangements and agreements need to be changed. We expect such arrangements and agreements to be **[31,727]** modified by the dates indicated in this Rule.

[415]The Commission did not define what it meant by "power pools" in the NOPR discussion. We use the term power pool in a very broad context here and have generally characterized three broad types of arrangements that represent some form of pooling: "tight pools", "loose" pools and other multilateral coordination arrangements, and holding companies. Even between the categories of tight and loose pools, however, there is no bright dividing line.

However, if necessary, we will institute section 206 proceedings against public utilities that do not make such filings.

The Commission's technical conferences on power pools, ISOs, and pro forma tariffs made clear to us the need to articulate guidance in this Rule on the restructuring or modification of unduly discriminatory coordination arrangements -- particularly tight power pools.[416] They also made clear that members of tight power pools, in particular, need time to make the necessary modifications to these arrangements. We recognize that members of some power pools are already in the process of formulating voluntary modifications to pooling agreements to be filed with the Commission (e.g., PJM, NYPP, NEPOOL). Therefore, we will provide adequate time for these filings as well as guidance to changes that need to be made.

In addition, although we do not at this time find it necessary to require power pools to form an independent system operator in order to remedy undue discrimination, we believe ISOs may prove to be an effective means for accomplishing comparable access.[417] We recognize that

---

[416]A technical conference on pro forma tariffs was held on October 27, 1995. A technical conference on power pools was held on December 5 and 6, 1995 and a follow-up technical conference on ISOs and power pools was held on January 24, 1996.

[417]The DOJ and DOE suggested that the Commission examine operational unbundling as a way of enforcing comparability in transmission service. DOJ and DOE believe that functional unbundling may not be adequate to ensure comparability

several utilities are exploring the possibility of forming ISOs. For example, discussions are ongoing in California, PJM, NYPP, and the Midwest. Therefore, because of the industry's interest (which we share) in the concept of an ISO and the potential for an ISO to provide non-discriminatory transmission services to all market participants, we will provide guidance in this section on minimum ISO characteristics.

1. Tight Power Pools

For purposes of this Rule, the tight power pools are: New York Power Pool (NYPP), New England Power Pool (NEPOOL), Pennsylvania-New Jersey-Maryland Interconnection (PJM), and the Michigan Electric Coordinated Systems (MECS).

Public utilities who are members of a tight pool must file, within 60 days of publication of the Final Rule in the Federal Register, either: (1) an individual Final Rule pro forma tariff; or (2) a joint pool-wide Final Rule pro forma tariff. They are not required to take service for pool transactions under the tariff that is filed within 60 days. However, they will be required to file a joint pool-wide Final Rule pro forma tariff no later than December 31, 1996, and must begin to take service under that tariff for all pool

---

and so have recommended that some form of operational unbundling be required. While we believe that requiring this is premature, we note that an ISO is one way to achieve operational unbundling and we encourage the voluntary development of ISOs.

transactions no later than December 31, 1996. The purpose of this extension is to allow sufficient time for tight pools to amend their pooling agreements and to restructure their operations to conform to the requirements of the Final Rule. We also believe that the additional time is necessary to preserve efficient trading arrangements during the restructuring period.

The Commission therefore will require that the public utility members of tight pools file reformed power pooling agreements no later than December 31, 1996. The reformed power pool agreements should establish open, non-discriminatory membership provisions (including establishment of an ISO, if that is a pool's preferred method of remedying undue discrimination) and modify any provisions that are unduly discriminatory or preferential. The membership provision must allow any bulk power market participant to join, regardless of the type of entity, affiliation, or geographic location.

If the reformed agreement allows members to make transmission commitments or contributions in exchange for the discounted transmission rates, the pool may file a transmission tariff that contains an access fee for non-transmission owning members or non-members, justified solely on the basis of transmission-related costs. Alternatively, the pool could make available **[31,728]** a transmission rate that is structured the same as the discounted rate (e.g., non-pancaked) but with a higher rate that is justified on the basis of transmission-related costs borne (or contributed) by the pool members. However, any such access fee or higher rate must be justified solely on the basis of transmission costs and cannot be tied to the costs of any other

agreement among the pool members (e.g., generation reserve sharing).

2. Loose Pools

For purposes of the Final Rule, a loose pool is any multi- lateral (more than 2 public utilities) arrangement, many of which contain discounted and/or special transmission arrangements. Examples are MAPP, Inland Power Pool, and the MOKAN pool. Other entities may qualify to be treated as a loose pool if they can show that they meet the definition above.

Public utilities within a loose pool must file, within 60 days of publication of the Final Rule in the Federal Register, either: (1) an individual Final Rule pro forma tariff; or (2) a pool-wide Final Rule pro forma tariff. They are not required to take service for pool transactions under the tariff that is filed within 60 days. However, they will be required to file a joint pool-wide Final Rule pro forma tariff no later than December 31, 1996, and must begin to take service under that tariff for all pool transactions no later than December 31, 1996. The purpose of this extension is to allow sufficient time for loose pools to amend their agreements and to restructure their operations to conform to the requirements of the Final Rule. We also believe that the additional time is necessary to preserve efficient trading arrangements during the restructuring period.

The Commission therefore will require that the public utility members of loose pools file reformed power pooling agreements no later than December 31, 1996. They also must file a joint pool-wide tariff no later than December 31, 1996.

The reformed power pool agreements should establish open, non-discriminatory membership provisions and modify any provisions that are unduly discriminatory or preferential. The membership provision must allow any bulk power market participant to join, regardless of the type of entity, affiliation, or geographic location.

The Commission recognizes that loose pools typically do not operate as a single control area and that operational unbundling, perhaps through an ISO, might not be readily attainable at this time. Nonetheless, we encourage the members of loose pools to explore the advantages of the ISO concept.

If the reformed agreement allows members to make transmission commitments or contributions in exchange for discounted transmission rates, the pool may file a transmission tariff that contains an access fee for non-transmission owning members or non-members, justified solely on the basis of transmission-related costs. Alternatively, the pool could make available a transmission rate that is structured the same as the discounted rate (e.g., non-pancaked) but with a higher rate that is justified on the basis of transmission-related costs borne (or contributed) by the pool members. However, any such access fee or higher rate must be justified solely on the basis of transmission costs and cannot be tied to the costs of any other agreement among the pool members (e.g., generation reserve sharing).

3. Public Utility Holding Companies

Public utility members of registered and exempt holding companies that are also members of tight or loose

pools are subject to the tight and loose pool requirements set forth above. The remaining holding company public utility members, with the exception of the Central and South West (CSW) System, are required to file a single system-wide Final Rule pro forma tariff permitting transmission service across the entire holding company system at a single price within 60 days of publication of the Final Rule in the Federal Register (service companies may, of course, file on behalf of their public utility affiliates). As discussed below, CSW presents special circumstances.

The CSW System is comprised of four operating public utilities. Two of those utilities, Southwestern Electric Power Company (SWEPCO) and Public Service Company of Oklahoma (PSO) operate in the Southwest Power Pool (SPP). The other two, West Texas Utilities Company (West Texas) and Central Power and Light Company (CP&L), operate in the Electric Reliability Council of Texas (ERCOT). SWEPCO and PSO exchange power with West Texas and CP&L **[31,729]** through two high voltage, direct current interconnections (the North and East Interconnections).[418]

Pursuant to the Commission orders concerning the North and East Interconnections, CP&L, West Texas, SWEPCO, and PSO have on file what are referred to as the

---

[418]The North and East Interconnections were ordered by the Commission pursuant to sections 210, 211 and 212 of the Federal Power Act. See *Central Power and Light Company, et al.*, 17 FERC ¶61,078 (1981), order on reh'g, 18 FERC ¶61,100 (1982); 40 FERC ¶61,077 (1987).

"to or from and over tariffs."[419] Those tariffs apply only to transmission service that involves the delivery of power and energy to or from and over the North and East Interconnections.[420] The tariffs do not apply to the transmission of power for CSW subsidiaries other than the operating companies. The tariffs in many respects are different from the Final Rule pro forma tariff and do not provide comparable services. Moreover, the pricing provided in the "to or from and over" tariffs is different from the pricing set forth in the Texas Commission's final open access rule.[421]

Given these special circumstances, we believe it appropriate to give CSW the opportunity to propose a solution to achieving comparability for the CSW system. Accordingly,

---

[419]Houston Lighting and Power Company (HL&P) and Texas Utilities Electric Company (TU) also have on file "to or from and over tariffs" pursuant to the Commission orders.

[420]*See, e.g.*, CP&L and West Texas Interpool Transmission Service Tariff, §4.1.

[421]Compare 21 TEX REG 1397, LEXIS, mimeo at p. 18 (adopting hybrid pricing scheme with 70% of transmission rate based on regional postage stamp method and 30% based on the vector-absolute megawatt-mile method) with Id. at Article III.

We note that the Texas Commission concluded that the ERCOT portion of the costs of the North and East Interconnections "should be included in the cost of service, when the owners of the (Interconnections) amend the FERC tariffs for the use of the (Interconnections) to provide equal access to other utilities. 21 TEX REG, LEXIS, mimeo at p. 24.

we direct the public utility subsidiaries of CSW to consult with the Texas, Arkansas, Oklahoma and Louisiana Commissions and to file not later than December 31, 1996 a system tariff that will provide comparable service to all wholesale users on the CSW System,[422] regardless of whether they take transmission service wholly within ERCOT or the SPP, or take transmission service between the reliability councils over the North and East Interconnections.[423]

The Commission will give public utilities that are members of holding companies an extension of the requirement to take service under the system tariff for wholesale trades between and among the public utility operating companies within the holding company system. This extension is until December 31, 1996 -- the same extension we are granting to power pools. At that point, the public utility operating companies will be required to take service

---

[422]It may be appropriate to have different rates for transmission service wholly within ERCOT or the SPP, and for service between the reliability councils. However, the same rates, terms, and conditions applicable for third parties should also be applicable to the CSW System's wholesale transmission requirements.

[423]We recognize that this action may require amendment to the Commission's orders under FPA sections 210, 211, and 212, ordering the North and East Interconnections. In this regard, it should be clearly understood that the Commission's action in requiring comparable service by the CSW System is not in any way intended to result in public utility status to any ERCOT participants that are not public utilities -- e.g., HL&P and TU. See 16 U.S.C. 824(b)(2).

under the Final Rule pro forma tariff for wholesale trades among themselves. In addition, it may be necessary for registered holding companies to reform their holding company equalization agreement to recognize the non-discriminatory terms and conditions of transmission service required under the Final Rule pro forma tariff.

4. Bilateral Coordination Arrangements

Any bilateral wholesale coordination agreement executed after the effective date of this Rule will be subject to the functional unbundling and open access requirements set forth in this Rule. With regard to existing bilateral agreements, however, the diversity of the types of agreements currently on file presents special implementation problems. The Commission is particularly concerned with future economy energy transactions that may occur pursuant to existing umbrella-**[31,730]**type coordination agreements. Accordingly, we shall require all bilateral economy energy coordination contracts executed before the effective date of this Rule to be modified to require unbundling of any economy energy transaction occurring after December 31, 1996. All non- economy energy bilateral coordination contracts executed before the effective date of this Rule will be permitted to continue in effect, but will be subject to complaints filed under section 206 of the FPA. Under those procedures, the rates, terms, and conditions of individual coordination contracts may be challenged as unduly discriminatory or otherwise unlawful.

To compute the unbundled coordination compliance rate, the utility must subtract the corresponding transmission unit charge in its open access tariff from the existing

coordination rate ceiling. For example, if a utility has a coordination rate ceiling for hourly service of incremental cost plus 15 mills/kWh and a transmission tariff rate for hourly service of 3 mills/kWh, it shall revise the coordination rate ceiling to incremental cost plus 12 mills/kWh. The Commission cautions that the compliance filing will be strictly limited to removing the current transmission tariff price from the coordination price and will not be a medium for otherwise revising the residual coordination sales price.

The transmission rate for the coordination transactions may be at or below the tariff rate. However, if a utility's transmission operator offers a discounted transmission rate to the utility's wholesale marketing department or an affiliate for the purposes of coordination transactions, the same discounted rate must be offered to others for trades with any party to the coordination agreement. In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory.[424] This may require parties to file modifications of the coordination arrangements.

ISO Principles

The Commission recognizes that some utilities are exploring the concept of an Independent System Operator and that the tight power pools are considering restructuring proposals that involve an ISO. While the Commission is not requiring any utility to form an ISO at this time, we wish to encourage the formation of properly-structured ISOs. To this

---

[424]All discounts must be posted on the transmission provider's OASIS.

end, we believe it is important to give the industry some guidance on ISOs at this time. Accordingly, we here set out certain principles that will be used in assessing ISO proposals that may be submitted to the Commission in the future.

These principles are applicable only to ISOs that would be control area operators, including any ISO established in the restructuring of power pools. We recognize that some utilities are exploring concepts that do not involve full operational control of the grid. Without in any way prejudging the merits of such arrangements, the following principles do not apply to independent administrators or coordinators that lack operational control. We do not have enough information at this time to offer guidance about such entities, but recognize that they could perform a useful role in a restructured industry.

Because an ISO will be a public utility subject to our jurisdiction,[425] the ISO's operating standards and procedures must be approved by the Commission. In addition, a properly constituted ISO is a means by which public utilities can comply with the Commission's non-discriminatory transmission tariff requirements. The principles for ISOs are:

1. The ISO's governance should be structured in a fair and non-discriminatory manner. The primary purpose of an

---

[425]A public utility is any person that owns or operates facilities used for the transmission of electric energy in interstate commerce or the sale of electric energy at wholesale in interstate commerce. An ISO will operate facilities used for the transmission of electric energy in interstate commerce and thus will be subject to the Open Access and OASIS rules.

ISO is ~~to~~ ensure fair and non-discriminatory access to transmission services and ancillary services for all users of the system. As such, an ISO should be independent of any individual market participant or any one class of participants (e.g., transmission owners or end-users). A governance structure that includes fair representation **[31,731]** of all types of users of the system would help ensure that the ISO formulates policies, operates the system, and resolves disputes in a fair and non-discriminatory manner. The ISO's rules of governance, however, should prevent control, and appearance of control, of decision-making by any class of participants.

2. An ISO and its employees should have no financial interest in the economic performance of any power market participant. An ISO should adopt and enforce strict conflict of interest standards. To be truly independent, an ISO cannot be owned by any market participant. We recognize that transmission owners need to be able to hold the ISO accountable in its fiduciary role, but should not be able to dictate day-to-day operational matters. Employees of the ISO should also be financially independent of market participants. We recognize, however, that a short transition period (we believe 6 months would be adequate) will be needed for employees of a newly formed ISO to sever all ties with former transmission owners and to make appropriate arrangements for pension plans, health programs and so on. In addition, an ISO should not undertake any contractual arrangement with generation or transmission owners or transmission users that is not at arm's length. In order to ensure independence, a strict conflict of interest standard should be adopted and enforced.

3. An ISO should provide open access to the transmission system and all services under its control at non-pancaked rates pursuant to a single, unbundled, grid-wide tariff that applies to all eligible users in a non-discriminatory manner. An ISO should be responsible for ensuring that all users have non-discriminatory access to the transmission system and all services under ISO control. The portion of the transmission grid operated by a single ISO should be as large as possible, consistent with the agreement of market participants, and the ISO should schedule all transmission on the portion of the grid it controls. An ISO should have clear tariffs for services that neither favor nor disfavor any user or class of users.

4. An ISO should have the primary responsibility in ensuring short-term reliability of grid operations. Its role in this responsibility should be well-defined and comply with applicable standards set by NERC and the regional reliability council. Reliability and security of the transmission system are critical functions for a system operator. As part of this responsibility an ISO should oversee all maintenance of the transmission facilities under its control, including any day-to-day maintenance contracted to be performed by others. An ISO may also have a role with respect to reliability planning. In any case, the ISO should be responsible for ensuring that services (for all users, including new users) can be provided reliably, and for developing and implementing policies related to curtailment to ensure the on-going reliability and security of the system.

5. An ISO should have control over the operation of interconnected transmission facilities within its region. An

ISO is an operator of a designated set of transmission facilities.

6. An ISO should identify constraints on the system and be able to take operational actions to relieve those constraints within the trading rules established by the governing body. These rules should promote efficient trading. A key function of an ISO will be to accommodate transactions made in a free and competitive market while remaining at arm's length from those transactions. The ISO may need to exercise some level of operational control over generation facilities in order to regulate and balance the power system, especially when transmission constraints limit trading over interfaces in some circumstances. It is important that the ISO's operational control be exercised in accordance with the trading rules established by the governing body. The trading rules should promote efficiency in the marketplace. In addition, we would expect that an ISO would provide, or cause to be provided, the ancillary services described in this Rule.

7. The ISO should have appropriate incentives for efficient management and administration and should procure the services needed for such management and administration in an open competitive market. Management and administration of the ISO should be carried out in an efficient manner. In addition to personnel and administrative functions, an ISO could perform certain operational functions, such as: determination of appropriate system expansions, transmission **[31,732]** maintenance, administering transmission contracts, operation of a settlements system, and operation of an energy auction. The ISO should use competitive procurement, to the extent possible, for all services provided by the ISO that are

needed to operate the system. All procedures and protocols should be publicly available.

8. An ISO's transmission and ancillary services pricing policies should promote the efficient use of and investment in generation, transmission, and consumption. An ISO or an RTG of which the ISO is a member should conduct such studies as may be necessary to identify operational problems or appropriate expansions. Appropriate price signals are essential to achieve efficient investment in generation and transmission and consumption of energy. The pricing policies pursued by the ISO should reflect a number of attributes, including affording non-discriminatory access to services, ensuring cost recovery for transmission owners and those providing ancillary services, ensuring reliability and stability of the system and providing efficient price signals of the costs of using the transmission grid. In particular, the Commission would consider transmission pricing proposals for addressing network congestion that are consistent with our Transmission Pricing Policy Statement. In addition, an ISO should conduct such studies and coordinate with market participants including RTGs, as may be necessary to identify transmission constraints on its system, loop flow impacts between its system and neighboring systems, and other factors that might affect system operation or expansion.

9. An ISO should make transmission system information publicly available on a timely basis via an electronic information network consistent with the Commission's requirements. A free-flow of information between the ISO and market participants is required for an ISO to perform its functions and for market participants to efficiently participate in the market. At a minimum,

information on system operation, conditions, available capacity and constraints, and all contracts or other service arrangements of the ISO should be made publicly available. This information should be made available on an OASIS operated by the ISO.

10. An ISO should develop mechanisms to coordinate with neighboring control areas. An ISO will be required to coordinate power scheduling with other entities operating transmission systems. Such coordination is necessary to ensure provision of transmission services that cross system boundaries and to ensure reliability and stability of the systems. The mechanisms by which ISOs and other transmission operators coordinate can be left to those parties to determine.

11. An ISO should establish an ADR process to resolve disputes in the first instance. An ISO should provide for a voluntary dispute resolution process that allows parties to resolve technical, financial, and other issues without resort to filing complaints at the Commission. We would encourage the ISO to establish rules and procedures to implement alternative dispute resolution processes.

G. *Pro Forma Tariff*

In the NOPR, the Commission stated that --

all utilities use their own systems in two basic ways: to provide themselves point-to-point transmission service that supports coordination sales, and to provide themselves network transmission service that supports the economic dispatch of their own generation units and purchased power

resources (integrating their resources to meet their internal loads).[426]

Accordingly, the Commission proposed two pro forma tariffs in Appendices B and C of the NOPR: one for point-to-point service and one for network service. Our goal was to encourage the development of competitive bulk power markets by ensuring that all participants would be able to secure transmission services on a non-discriminatory basis. We attempted in the NOPR pro forma tariffs to articulate the minimally acceptable terms and conditions of service for point-to-point and network transmission service that were required to ensure non-discriminatory transmission service.[427] We explained that, for the most part, specific pricing provisions were omitted. We asked for **[31,733]** comments on whether these tariffs provided a good basis for defining the minimum acceptable non-price terms and conditions of service.[428]

Subsequently, in a June 28, 1995 order, we encouraged public utilities to file open access transmission tariffs as soon as possible.[429] Tariffs with terms and conditions of service substantively similar to the NOPR pro forma tariffs

---

[426]*FERC Statutes and Regulations* ¶32,514 at p. 33,079.

[427]*Id.* at p. 33,092.

[428]On October 27, 1995, the Commission's staff sponsored a technical conference on the pro forma tariffs.

[429]*American Electric Power Service Corporation, et al.*, 71 FERC ¶61,393, modified, 72 FERC ¶61,287 (1995).

would become effective without a refund condition, assuming there were no other concerns, e.g., rate issues. We also indicated that these tariffs would be subject to revision based on the Final Rule.

Unified Pro Forma Tariff

The Commission received many comments on both the point-to-point and network tariffs. Many commenters suggested improvements to the proposed tariffs. Others took issue with how to reconcile various aspects of service under the two tariffs (e.g., cost allocation, service priority, customer rights and obligations). As discussed below, the Commission has attempted to address these concerns in developing tariff requirements for the Final Rule. Importantly, while the Commission has retained point-to-point transmission service and network transmission service as distinct services, the requirements for the two services are now in a single pro forma tariff.[430] The Final Rule pro forma tariff eliminates many of the differences between the two NOPR pro forma tariffs, provides a unified set of definitions, and consolidates certain common requirements such as the obligation to provide ancillary services. The general terms and conditions of transmission service specified in the Final Rule pro forma tariff should be familiar to all utilities, particularly those that have voluntarily filed open access tariffs based on the NOPR pro forma tariffs.

---

[430]The Final Rule pro forma tariff is attached as Appendix D.

The Commission believes that the modified, single pro forma tariff, in conjunction with the other requirements, is sufficient to remedy undue discrimination in the provision of transmission services. However, we note that in an accompanying notice of proposed rulemaking in Docket No. RM96-11-000, we are seeking comments on whether a different form of open access tariff -- one based solely on a capacity reservation system -- might better accommodate competitive changes occurring in the industry while ensuring that all wholesale transmission service is provided in a fair and non-discriminatory manner.

We address below the comments received on the NOPR tariff and the specific modifications we have made in the Final Rule pro forma tariff.

1. Tariff Provisions That Affect The Pricing Mechanism

a. Non-Price Terms and Conditions Comments

Utilities For Improved Transition argues that any generic imposition of detailed tariffs on the electric industry will stifle the evolution of the industry. Rather, it asserts, utilities that supply transmission service should be permitted to apply general principles of comparability in their company-specific tariffs, using terms and conditions of service based on their own particular circumstances and those of their customers.

Utility Working Group wants the final rule to allow utilities to depart from the pricing method implicitly contained in the NOPR pro forma tariffs. It argues that the final rule

should recognize that some terms and conditions may not make sense in the context of innovative pricing proposals.

DOE thinks that it is proper to base the tariffs on a familiar and simple pricing method. However, DOE suggests that, in the future, the Commission carefully assess the workability of the contract path model in a competitive bulk power market. DOE suggests that spot or real-time pricing should be considered.

Numerous commenters contend that the NOPR pro forma tariffs are based upon the contract path, embedded cost methodology. According to EEI and other IOU commenters, conforming changes may be needed to various terms and conditions **[31,734]** of the tariffs to implement pricing methodologies that are not based upon contract path. These commenters argue that any flow-based model would necessitate different non-price terms and conditions. The commenters generally recognize the technical difficulties of implementing a flow-based model.[431] These commenters assert that the NOPR pro forma tariffs, as written, are not independent of pricing.

EGA criticizes the assumption underlying the contract path approach, i.e., that the capacities of individual transmission paths can be determined independently and made available to third parties. EGA notes that, in light of the competitive implications associated with transmission pricing, some utilities may propose other non-price terms and

---

[431] Additional comments concerning transition to flow-based pricing are summarized in Section IV.A.6.

conditions suitable for other pricing methods, including power-flow-based tariffs. EGA expresses concern that the pro forma tariffs will be the only type of tariff allowed. EGA believes that the Commission should follow its transmission pricing policy guidelines and not impose a special burden on parties proposing tariffs that differ from the final rule pro forma tariffs, including non-price terms that support alternative pricing methods.

Some commenters also interpret the lack of reference to opportunity cost and incremental cost in the NOPR pro forma tariffs as a rejection of their use.[432]

Commission Conclusion

We agree that non-price terms and conditions cannot be designed independent of pricing and cost recovery. As discussed in detail below, the Final Rule pro forma tariff is intended to initiate open access, with non-price terms and conditions based on the contract path model of power flows and embedded cost ratemaking. It is designed based on the practices and procedures currently used by virtually all public utilities and complements the large number of tariffs already filed with the Commission. The Final Rule pro forma tariff is not intended to signal a preference for contract path/embedded cost pricing for the future. We recognize that the industry, in response to changes in institutions, competitive pressure, and technological innovations, is evolving rapidly. For example, various forms of flow-based pricing are beginning to be

[432]*E.g.*, BPA, Utilities For Improved Transition, PG&E, Duke.

considered in conjunction with electronic transmission information systems. We seek to encourage this process and will in the future entertain non- discriminatory tariff innovations to accommodate new pricing proposals.[433]

In response to various comments, we are revising certain non-price terms and conditions where suggested changes either improve the tariff services or reconcile tariff inconsistencies. The nature of these tariff revisions does not appear to have serious cost consequences. The mandated changes are generally compatible with the rate proposals already filed by many public utilities. As discussed in Section IV.H., those utilities will not be required to file corresponding rate changes due to our mandated tariff changes to non-price terms and conditions, although they will be permitted to do so.

The Final Rule pro forma tariff includes specific terms and conditions rather than general principles. By initially requiring a standardized tariff,[434] we intend to foster broad access across multiple systems under standardized terms and conditions. However, in response to concerns raised by certain commenters, the tariff provides for certain deviations where it can be demonstrated that unique practices in a geographic region require modifications to the Final Rule pro

[433]We further clarify that, contrary to some commenters' interpretation, the Final Rule pro forma tariff is in no way a rejection of opportunity or incremental cost pricing.

[434]As noted in Section IV.H., public utilities may propose variations that are consistent with or superior to the terms and conditions in the Final Rule pro forma tariff.

forma tariff provisions. Accordingly, where applicable, the tariff permits the use of alternative non-price terms or conditions that are reasonable, generally accepted in the region, and consistently adhered to by the transmission provider.

Finally, we will allow utilities to propose a single cost allocation method for network and point-to-point transmission services. These principles, as well as other **[31,735]** modifications and clarifications to the NOPR pro forma tariffs, are discussed in detail below.

b. Load Ratio Sharing Allocation Mechanism for Network Service

Comments

Some commenters believe that load ratio cost allocation is appropriate for network service.[435] Other commenters argue that load ratio cost allocation is inappropriate, but disagree on the alternative. They offer a variety of other cost allocation and pricing methods.

The most frequent comment is that network and point-to-point services should be priced on the same basis. Florida Power Corp wants network contract demand to be offered and priced on a 12 CP basis.[436] ConEd and Duke argue that their

---

[435]*E.g.*, PSNM, WP&L.

[436]Florida Power Corp's contract demand proposal would allow a network customer to nominate less than its full load for transmission service.

systems are built and designed to meet a single peak; therefore, they contend that network service costs should be allocated with a load ratio calculation based on annual system peak rather than 12 CP. PSE&G claims that load ratio cost allocation works only if the customer has its own generation. Many commenters propose that "behind the meter" generation and load be eliminated from the network load ratio calculation.[437]

CINergy notes that the transmission provider's monthly load ratio calculation includes its long-term off-system firm service. It proposes that off-system sales be eliminated from the load ratio calculation to enable the transmission provider to offer discounts on long-term service. Alternatively, CINergy proposes that the revenues from these long-term off-system sales be shared with network customers based on their load ratio.

Atlantic City and Allegheny contend that cost allocation for network service should also reflect customers' relative energy use (i.e., not just customers' coincident demand). Consequently, these commenters propose that cost allocation consider the network customer's actual load factor. Allegheny also proposes adding a minimum revenue provision to the load ratio method to recognize cost responsibility for non-peak use. Allegheny further proposes to include an increasing return on equity as available transmission capacity decreases. EEI proposes that cost allocation be based on a customer's non-coincident peak demand.

---

[437]*E.g.*, Cajun, NRECA.

Lower Colorado River Authority proposes using load flow studies to determine planned use during the system peak with MW-mile billing units. It believes that this pricing method should be used for all transmission service to ensure comparable transmission pricing. Oklahoma G&E wants cost allocation to be based on the impacted MW-mile method, or alternatively, to determine embedded cost by voltage level. Centerior proposes the use of actual transfer capability instead of contract path capability in determining cost responsibility.

Orange & Rockland recommends some form of a "poolco" approach using locational marginal cost pricing. DOE also recommends using location-specific spot pricing (a form of marginal cost) for operating and congestion costs.

Public Generating Pool believes that load ratio share pricing is unworkable in the Pacific Northwest, in part because generation is generally located outside of the control area directly served by parties in the Northwest, and in part because BPA, which does not have a typical service territory, dominates the regional transmission market. Seattle states that cost allocation based solely on demand is inappropriate for systems that consist predominantly of hydro generation.[438]

AEC & SMEPA and NRECA are concerned about pancaked rates for network service that is provided to load served by more than one network tariff. Other commenters

[438]Additional comments concerning the Pacific Northwest are summarized in Section IV.K.

advocate use of some form of regional pricing.[439] American Wind proposes the use of a complex seasonal calculation, which appears to benefit wind energy. NY Com and Missouri-Kansas Industrials also express a preference for seasonal pricing models.

[31,736]

Commission Conclusion

We conclude that the load ratio allocation method of pricing network service continues to be reasonable for purposes of initiating open access transmission. Network service permits a transmission customer to integrate and economically dispatch its resources to serve its load in a manner comparable to the way that the transmission provider uses the transmission system to integrate its generating resources to serve its native load. Because network service is load based, it is reasonable to allocate costs on the basis of load for purposes of pricing network service. This method is familiar to all utilities, is based on readily available data, and will quickly advance the industry on the path to non-discrimination. We are reaffirming the use of a twelve monthly coincident peak (12 CP) allocation method because we believe the majority of utilities plan their systems to meet their twelve monthly peaks. Utilities that plan their systems to meet an annual system peak (e.g., ConEd and Duke) are free to file another method if they demonstrate that it reflects their transmission system planning. Moreover, we recognize that alternative allocation proposals may have merit and welcome

[439]*E.g.*, OH Coops, Municipal Energy Agency Nebraska, UT Com.

their submittal by utilities in future rate applications. They will be evaluated on a case-by-case basis and decided on their merits.

As to the concerns raised by AEC & SMEPA and NRECA about pancaked rates for network service provided to load served by more than one network service provider, we have stated that if a customer wishes to exclude a particular load at discrete points of delivery from its load ratio share of the allocated cost of the transmission provider's integrated system, it may do so.[440] Customers that elect to do so, however, must seek alternative transmission service for any such load that has not been designated as network load for network service. This option is also available to customers with load served by "behind the meter" generation that seek to eliminate the load from their network load ratio calculation.

As noted, the most frequent comment is that the network and point-to-point services should be priced on a similar basis. This concern is addressed in the next section.

* * * * *

[pp. 31,743 - 31,753]

[31,743]

g. Ceiling Rate for Non-Firm Point-to-Point Service

---

[440]*Florida Municipal Power Agency v. Florida Power & Light Company*, 74 FERC ¶61,006 (1996), reh'g pending.

Commenters generally support a ceiling rate for non-firm transmission service, capped at the firm rate.[453] Others request clarification as to whether the point-to-point tariff rates are fixed or are ceiling rates. Central Illinois Public Service's major concern is that, if the rates are fixed, the tariffs may result in higher prices for capacity and energy than those currently allowed for bundled service.

NYSEG argues that unequal pricing is a natural phenomenon of the open marketplace and requests assurance that offering transmission service at prices below a cost-based ceiling rate will not expose a transmission provider to claims of undue discrimination.

AEC & SMEPA opposes using the firm rate as the cap for non-firm transmission service. It states that, given the substantially lower quality of non-firm service (with no obligation to plan for such service), no cost-of-service principle justifies charging rates for non-firm service as high as the rate for firm service.

EGA and NRECA state that any discounts from the maximum firm rate must be uniform, transparent, readily understood, and posted on a RIN. According to CCEM and NRECA, the transmitting utility must have nondiscriminatory discount practices and must contemporaneously offer discounts to transmission customers at the same time and on the same basis as discounts for internal sales operations or affiliates. Commission Conclusion

---

[453]*E.g.*, Duke, SCE&G, AEP, FPL.

We believe that it is important to continue to allow pricing flexibility. In accordance with the Commission's current policies, the rate for non-firm point-to-point transmission service may reflect opportunity costs. Any provisions for opportunity cost pricing for non-firm service must meet the requirements already discussed. If a utility chooses to adopt opportunity cost pricing, the non-firm rate is effectively capped by the availability of firm service and is not subject to a separately-stated price cap. If a utility chooses not to adopt opportunity cost pricing, the non-firm rate is capped at the firm rate. We also wish to ensure that non-firm transmission service is priced in a nondiscriminatory fashion. Accordingly, if a transmission provider offers a rate discount to its affiliate, or if the transmission provider attributes a discounted rate to its own transactions, the same discounted rate must also be offered at the same time to non-affiliates on the same **[31,744]** transmission path and on all unconstrained transmission paths. We will further require that any affiliate discounts from the maximum firm rate must be transparent, readily understandable, and posted on the transmission provider's OASIS in advance so that all eligible customers have an equal opportunity to purchase non-firm transmission at the discounted rate.[454] In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory and must be reported on the OASIS within 24 hours of when

[454]The same requirements will apply to discounts from firm transmission service. Similarly, if a transmission provider offers an affiliate a discount for ancillary services, or attributes a discounted ancillary service rate to its own transactions, it must offer at the same time the same discounted rate to all eligible customers. Discounted ancillary services rates must be posted on the OASIS pursuant to new Part 37 of the Commission's regulations.

available transmission capability (ATC) is adjusted in response to the transaction. As discussed in the RIN section, information, including the price for all non-firm transaction discounts, must be posted on the OASIS to ensure comparability.

2. Priority For Obtaining Service

The term "priority" is used in the comments in several senses. The intent of the comment depends on which kind of "priority" is intended. In general, there are comments about the order in which parties can obtain new service, which we call "reservation priority," and there are comments about the order in which parties lose service they already have, which we call "curtailment priority." Commenters may establish different reservation priorities for various services, such as network, off-system sales, firm, ability to reserve a portion of new transmission capacity to be constructed, and so on. Curtailment priorities also differ with the type of service. However, many commenters assert that certain parties should or should not have "priority" without distinguishing the kind of priority or type of service for which priority is intended.

a. Reservation Priority for Existing Firm Service Customers

Many IOUs, state commissions, and cooperatives strongly believe that native load should have priority to reserve transmission capacity under the tariffs.

EEI suggests that existing and future allocations of transmission capacity must be based on proper transmission pricing or, in its absence, priority of service. According to EEI, retail and existing wholesale requirements service should

have the highest priority for use of transmission capacity, followed by long-term point-to-point service. Dayton P&L supports a continued preference for native load growth because native load customers have borne the majority of the costs of the transmission system. Detroit Edison, EEI, and Florida Power Corp claim that, because native load and network customers pay higher rates during all hours, such customers should have higher priority for service requests than others requesting transmission service. These commenters also claim that the transmission provider should be able to reserve firm capacity for native load and network service customers.

Similarly, NARUC wants wholesale and retail native load customers to be held harmless from functional unbundling of wholesale transmission services. Because these customers have borne the vast majority of the costs of the utility's transmission facilities, NARUC argues that priority of service, quality of service, and allocation of joint and common costs to native load customers should not be affected by the transition to an open access transmission regime.

PA Com does not share the Commission's concern that a transmission provider may discriminate against a third party transmission customer vis-a-vis native load. It finds nothing impermissible in this sort of discrimination, arguing that the interconnected system was financed by, designed for, and built to serve native load.

NRECA explains that most transmission customers that seek network service will already be receiving similar service (albeit in a bundled form) from their transmission providers. It argues that these customers should receive the

same priority of service as the transmission provider's native load customers for as long as they continue to take network service, whether under a current bundled wholesale **[31,745]** supply contract, a private transmission contract, or a network tariff.[455]

East Kentucky requests that the final rule clarify that member distribution cooperatives of G&Ts will have priority over third parties in the use of the G&T's existing transmission facilities. TVA comments that native load customers and emergency service to neighboring systems should have a higher service priority than transmission services sold to third parties (where an alternative power supply is available to the third party).

Commission Conclusion

We reiterate that we are not requiring the transmission provider to unbundle transmission service to its retail native load nor are we requiring that bundled retail service be taken under the terms of the Final Rule pro forma tariff. However, the amount of transmission capacity available to wholesale and unbundled retail customers under the Final Rule pro forma tariff is clearly affected by the amount of transmission capacity that the transmission provider reserves for the use of its native load customers and the future load growth of those customers. The transmission provider may reserve in its calculation of ATC transmission capacity necessary to accommodate native load growth reasonably forecasted in its planning horizon. However, the transmission provider is

---

[455]See also American Forest & Paper, AMP-Ohio.

obligated to provide transmission service to others under the Final Rule pro forma tariff out of capacity reserved for native load growth up to the time the capacity is actually needed for such future needs. Furthermore, as we explained previously, while existing wholesale customers do not have any ownership-like rights to the capacity they used during the term of their contract, they will have a right of first refusal to that capacity after the expiration of their contracts or when their contracts become subject to renewal or rollover.[456]

b. Reservation Priority for Firm Point-to-Point and Network Service

A number of commenters argue that all firm service should not be treated equally. These commenters argue that the price of the service should determine the priority that the service receives. A large number of IOUs and potential network customers (existing requirements customers) argue that in light of the pricing implicit in the NOPR, (i.e., 12 CP for network versus annual system peak for point-to-point) network service should have priority over point-to-point service (because, all other things being equal, the price for network service will be higher).

BG&E believes that a customer receiving service priority equal to native load and network customers should pay comparable rates. Thus, BG&E argues that either flexible firm point-to-point service should be priced the same as network service, or point-to-point service should have a lesser

[456]See discussion in Section IV.A.5.

priority than native load and network service customers if point-to-point service is priced lower than network service.

DE Muni believes that native load and network customers must have priority access to interfaces (particularly where they are constrained) after system reliability concerns have been satisfied. The same argument is advanced by commenters concerning long-term service versus short-term service. Public Generating Pool argues that long-term service should always have priority over short-term service because long-term customers contribute more towards fixed-cost recovery than do short-term customers.

Cajun objects to having its service and service to its customers, which it characterizes as network service, receive the same priority as firm point-to-point service customers who take service for periods as short as one hour. Cajun points out that it, as well as other network and native load customers, have been paying and will be paying for the transmission facilities in place to serve their needs for many years. According to Cajun, the transient firm point-to-point customer should not have equal standing. Cajun suggests, however, that a long-term firm point-to-point customer taking service for ten years or more should have service priority equal to native load and network service customers.

SC Public Service Authority argues that the availability of short-term firm service with a priority equal to long-term service would provide a means for short-term **[31746]** customers to obtain the advantages of long-term firm service at a much lower total cost. As a result, it argues that a few point-to-point customers would opt for long-term firm

service, and the burden of the residual costs of the transmission system would fall on network customers.

EEI claims that priority for point-to-point service should be on a continuum of firmness, with reservation (as well as curtailment) priority based upon duration of service and specific negotiated terms. EEI proposes that the point-to-point tariff be modified to provide a first-tier category of flexible point-to- point transmission service that is comparable in priority, price, length, and terms of service to network service. EEI believes that this modification will resolve the problems that are associated with establishing priorities between network service and point-to-point service if the Commission retains different CP cost allocation methods for each service.

On the other hand, CCEM, a group of power marketers, supports the concept that all firm service should be treated equally, regardless of the term or the nature of service.

Commission Conclusion

An essential element of non-discriminatory transmission access is the right of transmission customers to reserve and purchase transmission service that is of the same quality as that used by the transmission provider in serving its wholesale requirements customers and retail load. Thus, we reject the proposal of some commenters that transmission providers need not provide firm point-to-point service that is of the same "firmness" as the transmission provider's service to native load. However, the fact that both network service and point-to-point service are provided on an equally firm

basis does not mean that both types of service must be priced or reserved in the same manner.

The comments about reservation priorities for firm services boil down to two concerns. First, due to the differences in pricing firm point-to-point service and network service implicit in the NOPR (i.e., twelve-monthly CP pricing for network versus annual system peak for point-to-point), some commenters believe that network service should have priority over point-to-point service. Second, some commenters maintain that according firm, short-term point-to-point service a priority equal to long-term service provides a means for short-term customers to avoid making a fair contribution to the long-term costs of the system.

With respect to the first concern, we have eliminated the differences in pricing by permitting utilities to adopt point-to-point reservations as the customer load. As discussed above, for purposes of the Final Rule pro forma tariff, utilities are free to propose a single cost allocation method for the two services.

The second area of concern arises because of the first-come first-served reservation priority in the NOPR point-to-point tariff. The Commission recognizes that the tariffs, as proposed in the NOPR, provide the opportunity for a customer to reserve certain valuable rights (e.g., the right to short-term firm service during peak periods) while avoiding in part the long-term costs of the system (perhaps by relying on non-firm service during lengthy off-peak periods when there is a substantially reduced chance of interruption). However, the Commission has a countervailing concern that the transmission provider should not be able to withhold

valuable transmission capacity from potential customers if that capacity is not being used by those who are paying for the long-term costs of the system.

Accordingly, the Final Rule pro forma tariff provides a mechanism to address this concern while safeguarding the rights of potential customers to obtain access to unused capacity. The tariff provides that reservations for short-term firm point-to-point service (less than one year) will be conditional until one day before the commencement of daily service, one week before the commencement of weekly service, and one month before the commencement of monthly service. These conditional reservations may be displaced by competing requests for longer-term firm point-to-point service. For example, a reservation for daily firm point-to-point service could be displaced by a request for weekly firm point-to-point service during an overlapping period. Before the applicable reservation deadline, a holder of a conditional firm point-to-point reservation would have the right of first refusal to match any longer-term firm point-to-point reservation before being displaced. After the deadline, the reservation becomes **[31,747]** unconditional, and the service would be entitled to the same priorities as any long-term point-to-point or network firm service.[457]

The Final Rule pro forma tariff does not propose point-to-point or network service with various degrees of firmness beyond the simple categories of firm and non-firm. When a customer requests firm transmission service,

---

[457]The service itself, as opposed to reservations, is subject to the curtailment provisions discussed below.

reservation priorities are established based first on availability, and in the event the system is constrained, based on duration of the underlying firm service request; customers may choose the "firmness" of service they want by electing to take non-firm service, or by reserving and paying for firm service. We have not included any degrees of firmness in the Final Rule pro forma tariff because having intermediate categories of firmness under point-to-point or network service would, we believe, unnecessarily complicate the priority system. However, utilities are free to propose and fully support different reservation priority provisions for firm service in subsequent rate filings as long as those provisions are not unduly discriminatory, fully comply with the principles of comparability, and are priced appropriately.

c. Reservation Priorities for Non-Firm Service

IOUs, state commissions, and potential network customers tend to support the service reservation priorities for non-firm service set forth in the NOPR pro forma tariffs (i.e., transmission service by network customers for economy purchases to serve network load has a higher priority than non-firm point-to-point service, which has a higher priority than a firm point-to-point customer using transmission service at secondary points of receipt and delivery). However, because network customers pay a higher rate than point-to-point customers, these commenters argue that network customers should be permitted to use their off-peak load ratio share of the transmission system to make off-system sales. Many commenters argue that point-to-point customers can use their secondary service for both purchases and sales; thus, they believe it is discriminatory to limit network customers to purchases at secondary points.

Commenters that are opposed to the service reservation priority scheme in the NOPR pro forma tariffs argue that transmission providers will discriminate against third party users in favor of their native load economy purchases. These commenters argue that all non-firm service should have equal priority.

Other commenters, such as CINergy, would base priority on the duration of service. CINergy claims that this method would eliminate what it claims is an advantage (over network) given in the NOPR to point-to-point service in making short-term purchases. TVA notes that it establishes priority for non-firm service based on duration of service requested, with customers in each service category receiving priorities based on the rate they wish to pay.

Some commenters believe that the transmission price should affect the priority of customers to obtain non-firm transmission capacity.[458] However, other commenters argue that this seems to be precluded by the NOPR pro forma tariffs' service priority provisions.

Although PSE&G believes that the NOPR pro forma tariffs suggest a first-come, first-served allocation method for capacity in excess of that needed for firm transmission service, it proposes a fixed period of time for all potential users to submit bids for service (e.g., one week prior for monthly service), allowing the bid price to determine priority (i.e., the higher bid prices receive service priority over lower bid prices). According to PSE&G, customers could bid an "up

[458] *E.g.*, Duke, Orange & Rockland.

to" rate subject to a price floor, with all revenues flowed back to firm service customers. TVA also advocates departing from the first-come, first-served approach for allocating some uses of the transmission system, claiming that price is an effective means to establish priority for non-firm and short-term firm services.

Utility Wind Interest Group requests that non-firm service used for transmitting renewable resources be given a higher priority than non-firm service used **[31,748]** for transmitting conventional resources because renewable resources cannot store their fuel supply. Commission Conclusion

We continue to believe that network economy purchases should have a reservation priority over non-firm point-to-point and secondary point-to-point uses of the transmission system. Network transmission customers are obliged to pay all of the costs of the transmission system without regard to the resources from which energy is scheduled. Therefore, it is appropriate that the transmission associated with a network customer's economy purchases (i.e., transmission that is used to substitute one resource for another on an as-available basis) enjoys a higher priority than non-firm point-to-point transmission service.

Regarding the reservation priority for non-firm service under point-to-point service, we will adopt a reservation priority based upon duration of non-firm service, with price acting as a tie-breaker for competing service requests of an equal duration. If there is insufficient transmission capacity to accommodate all non-firm transmission requests, the reservation of longer duration should displace the shorter. For

example, a reservation for a month of non-firm service will displace a reservation for a week of non-firm service. Also, a reservation for a week will displace a reservation for a day, which will displace a reservation for an hour of non-firm service. If a customer requests non-firm and later another customer requests longer-term non-firm service before either term of service begins, the first customer to request service has the right of first refusal to change its request to the longer term of service. A firm point-to-point customer's use of transmission service at secondary points of receipt and delivery will continue to have the lowest reservation priority.

3. Curtailment Provisions

a. Pro-Rata Curtailment Provisions

A large number of IOUs that are control area operators argue for discretion to curtail the transaction that most effectively relieves the constraint, in lieu of mandatory pro-rata curtailments, which they argue are inappropriate and not cost effective.

Other commenters that do not support pro-rata curtailment argue that preference should be given to native load or existing customers because these customers have paid the majority of the costs of the transmission system. A large number of customers note that their existing contracts contain "enhanced" curtailment priorities (i.e., service to others will be curtailed before service to customers with such curtailment

priority) due to the large capital outlays made by them in connection with their service.[459]

Public Generating Pool believes that the proposed curtailment provisions may not be flexible enough for transactions in the Northwest. It argues that hydro spill should be avoided, and suggests that transactions from federal and/or non-federal hydroelectric generation facilities should not be curtailed pro rata with other transactions that do not rely on such facilities. Public Generating Pool urges that regional agreements (e.g., regional transmission group agreements) that would achieve this goal should be given deference.

Other commenters support pro-rata curtailments for firm service.[460] PSNM states that this has been its operating practice in the past, and PSNM expects to continue such an approach in the future.

Power marketer commenters generally support the pro-rata curtailment adding that a standardized curtailment priority applied nationally would provide greater open access and eliminate discriminatory curtailments.

Commenting on a related subject, EEI maintains that the network tariff provision for termination of service in the event a customer fails to curtail load[461] may not be realistic for

---

[459] *E.g.*, TANC, Turlock, SMUD.

[460] *E.g.*, PSNM and Nebraska Public Power District.

[461] Proposed Pro Forma Network tariff section 9.7 - System Reliability.

service to a Transmission Dependent Utility. EEI suggests that the Commission supplement this provision with a substantial penalty provision, coupled with an indemnification requirement.

[31,749]
Commission Conclusion

It was not our intent in the NOPR to require all transactions to be curtailed on a pro-rata basis regardless of whether the transaction relieves a constraint. We intended to permit curtailments of transactions that substantially relieve a constraint.[462] We intended and continue to believe that curtailment on a pro-rata basis is appropriate for curtailing the transactions that substantially relieve the constraint. In order to allay the concerns of the commenters addressing this issue,

---

[462]The Final Rule pro forma tariff contains language allowing the transmission provider the discretion to interrupt firm transmission service in an emergency or other unforeseen condition in a manner suggested by these commenters. Section 11.6, Curtailment of Firm Service, of the Final Rule pro forma tariff provides:

However, the Transmission Provider reserves the right to interrupt, in whole or in part, firm Transmission Service provided under this Tariff when, in the Transmission Provider's sole discretion, an emergency or other unforeseen condition impairs or degrades the reliability of its transmission system.

The reference to curtailments being allocated on a proportional (pro rata) basis addresses situations where multiple transactions could be curtailed to relieve a constraint.

we are clarifying the curtailment provision of the tariff to explicitly allow the transmission provider discretion to curtail the services, whether firm or non-firm, that substantially relieve the constraint. Of course, any curtailment must be made on a non-discriminatory basis, including curtailment of the transmission provider's own use of the transmission system. Customers that believe the curtailment policy is administered unfairly may file a section 206 complaint at the Commission.

Concerning the request of certain Pacific Northwest commenters, we would consider granting deference to an alternative curtailment method to avoid hydro spill if such a regional practice is generally accepted and adhered to across the region, as discussed further in Section IV.K.

Finally, we agree with EEI's observation that terminating network service under the tariff to a transmission dependent utility that fails to curtail load as required may not be appropriate. As a result, we clarify that under network and point-to-point service, the transmission provider may propose a rate treatment (penalty provision) to apply in the event a customer fails to curtail load as required under the Final Rule pro forma tariff. Such proposals will be evaluated on a case-by-case basis on compliance.

b. Curtailment Provisions for Non-Firm Service

A number of commenters seek clarification of the curtailment provision for non-firm service under the two tariffs. They note that economy purchases by the network customer are accorded a higher curtailment priority than non-firm service under the point-to-point tariff. However, under

the point-to-point tariff there is no acknowledgement of this higher priority for network service. Curtailments for non-firm transmission service under the point-to-point tariff are simply based upon duration of service, without reference to a higher priority for network economy purchases.

A number of commenters, including Industrial Energy Applications, suggest that a price-based curtailment queue for non-firm transmission will facilitate economy energy deals in highly competitive wholesale power supply markets and allow the parties to directly address delivery risk through the pricing mechanism.

Blue Ridge argues that the final rule should provide equal curtailment priority for all types of non-firm transmission service. Utilities For Improved Transition argues that network customers should be able to transmit non-firm power imports under the network tariff with the same curtailment priority that is assigned to all other firm network uses of the transmission system.

A number of commenters note that the tariffs allow non-firm service to be interrupted only for emergency or reliability reasons or to provide firm service. These commenters contend that, under this requirement, curtailment of non-firm service is unlikely.[463] As a result, they believe that non-firm service is elevated to firm service. To remedy this situation, these commenters argue that transmission

[463] *E.g.*, Florida Power & Light Company, Southern California Edison Company.

providers should have the ability to **[31,750]** curtail non-firm service for any economic reason.

Commission Conclusion

We have clarified in the Final Rule pro forma tariff that a network customer's economy purchases have a higher curtailment priority than non-firm point-to-point transmission service.

A higher curtailment priority should be provided to network economy energy purchases for the reasons stated in AES Power, Inc..[464] In that case, we recognized that the network transmission customer has already "paid" for the transmission of its economy purchases (i.e., transmission that is used to substitute one resource for another on an as available basis) through its payment of a load ratio share of the system.

Many commenters oppose the point-to-point service provision allowing non-firm service to be interrupted only for emergency or reliability reasons or to provide firm service. Upon further consideration, we agree that this provision is too narrow. Accordingly, the Final Rule pro forma tariff is revised to allow the transmission provider to curtail non-firm service for reliability reasons or economic reasons (i.e., in order to accommodate (1) a request for firm transmission service, (2) a request for non-firm service of greater duration, (3) a request for non-firm transmission service of equal

[464] 69 FERC ¶61,145 at p. 62,300 (1994) (proposed order), 74 FERC ¶61,220 (1996) (final order).

duration with a higher price, or (4) transmission service for economy purchases by network customers from non-designated resources.). However, all curtailments must continue to be made on a non-discriminatory basis including curtailments of the transmission provider's own non-firm uses of the transmission system under the tariff. A firm point-to-point customer's use of transmission service at secondary points of receipt and delivery will continue to have the lowest curtailment priority.

4. Specific Tariff Provisions

a. Network and Point-to-Point Customers' Uses of the System

Generally, transmission providers argue that the tariffs give too much flexibility to customers, while transmission customers argue that even more flexibility is required. The arguments are generally tied to pricing rather than technical problems with providing any level of service.

A common transmission provider argument is that the proposed firm point-to-point tariff provides a premium service comparable to network service, but at a lower rate. It has been suggested that either the flexibility to use non-firm service at secondary points of receipt and/or delivery at no additional charge under the point-to-point tariff be eliminated or that point-to-point customers should pay a premium price for such flexibility.[465] Transmission providers generally argue that flexible point-to-point service puts the transmission owner

[465] *E.g.*, EEI, Utility Working Group, SoCal Edison.

and the network customer at a competitive disadvantage. They assert that the point-to-point customer is able to use non-firm transmission to reach secondary receipt and delivery points for both sales and purchases, but the network customer may use only non-firm transmission to reach secondary points for purchases. Thus, they argue, the flexible point-to-point users can sell non-firm power with a small or even no transmission component (because the underlying transmission is effectively free). Electric Consumers Alliance and Cajun believe that the owner and network customer competing for that sale should not be charged for the identical transaction. Absent a change to the point-to-point tariff, a number of transmission providers and state commissions (including Midwest Commissions) argue that to provide balance to the tariffs, the network tariff should permit the network customers to have non-firm transmission to secondary receipt and delivery points at no additional charge for both purchases and sales within its load-ratio transmission entitlement. Utilities For Improved Transition refers to this proposed network tariff modification as "headroom."

CCEM opposes the headroom concept, arguing that "free" use of capacity will give transmission providers an unfair competitive advantage. CCEM also cites Order No. 636 in support of its position.

Conversely, a number of customer groups believe the point-to-point tariff **[31,751]** should be made more flexible by broadly defining the concept of points of receipt and delivery. They argue that all points of connection between the transmitting utility and the purchasing utility should be treated as a single point of delivery (POD) or point of receipt

(POR).[466] In this manner, a customer would not have to pay for every point of receipt or point of delivery, but could select a contract demand level of service. The customer could then use the service at multiple points without incurring separate reservation charges for each point.

A number of commenters contend that the Commission should not force specific tariffs on public utilities in the Pacific Northwest due to their unique status.[467] In particular, NWRTA recommends that the final rule recognize that the Pacific Northwest's integrated transmission system, including large components owned by non-public utilities, was constructed to support a unique region-wide hydroelectric-dependent generating system. NWRTA recommends that the final rule be sufficiently flexible to accommodate these unique characteristics without prejudicing the interests of users or providers of transmission services.

Similarly, Public Generating Pool states that the NOPR pro forma network tariff departs from the status quo arrangements in the Northwest and is generally unworkable because generation is usually remote from the control area serving the network load and because BPA, which does not have a typical service territory, dominates the regional transmission market. Public Generating Pool suggests that the Commission require, and the region develop, a "generation integration'' transmission tariff that would offer network-type

---

[466] *E.g.*, Arkansas Cities, NRECA.

[467] *E.g.*, Public Power Council, Washington Water Power, NWRTA.

service to a source or sources of generation unbundled from the "network services" designed to integrate load. Similar contract demand network tariffs have already been proposed by some IOUs.

Commission Conclusion

We will not allow network customers to make off-system sales within the load-ratio transmission entitlement at no additional charge. Commenters have raised no new arguments to persuade us to do so, The primary purpose of network service is to integrate resources to serve loads. Use of transmission by network customers for non-firm economy purchases, which are used to displace firm network resources, must be accorded a higher priority than non-firm point-to-point service and secondary point-to-point service under the tariff. Off-system sales transactions. which are sales other than those to serve a network customer's native load, must be made using point-to-point service. They can be made on either a firm or non-firm basis.

A large number of transmission providers support the "headroom" concept, arguing that without it the flexible point-to-point service puts them at a competitive disadvantage. This would be true if a utility serving load were required to use network service exclusively, However, we do not require any utility to take network service to integrate resources and loads. If any transmission user (including the public utility) prefers to take flexible point-to-point service,[468] they are free to do so. Any point-to-point customer may take advantage of the secondary, non-firm flexibility provided under point-to-point service equally, on an as-available basis.

---

[468]*See Florida Municipal Power Agency v. Florida Power & Light Company*, 74 FERC ¶61,006 at p. 61,013 and n. 70 (1996).

b. Minimum and Maximum Service Periods

Commenters raise issues regarding the minimum term of one hour for firm point-to-point service. Their concerns center on price and priority. Transmission providers point out that their native load customers pay the fixed cost of the transmission system every hour of the year. They argue that comparability is not achieved by permitting others to have service for one hour with equal priority to native load and other long-term customers. Others worry that the one-hour minimum term will: (1) Promote the selective use of the transmission system: (2) impair the ability of a utility to plan its system; and (3) adversely impact longer term transactions.

Tallahassee and KY Com are concerned that one-hour firm service may encourage **[31,752]** speculative advance requests for service during the system peak day (Cajun refers to this as cream skimming). These commenters express concern that such requests could displace other valid transactions or constrain a corridor or interface to the detriment of network service or native load customers, Tallahassee proposes a one-day minimum term for firm service.[469]

East Kentucky is concerned that users of the transmission system could, under the Commission's proposed open-access rule, purchase short-term firm service during peak months in lieu of annual firm service to reduce expt:nses associated with the purchase of firm transmission service. By buying short-term firm service only during the peak months,

---

[469]See also VEPCO, CSW, NYSEG, WP&L.

an entity can significantly reduce its transmission expenses by purchasing non-firm service during off-peak months when the available transmission capacity far exceeds the demand on the transmission system. For this reason, some commenters request that short-term firm service be priced to generate revenues over the peak months equal to the charge for annual firm service.

Duke argues that, because all curtailments are equal, the addition of each one hour firm transaction will lower the reliability profile of native load customers and other customers with long-term commitments. It suggests that different classes of services be established that offer transmission customers the flexibility to obtain an intermediate level of transmission service (between native load firm and non-firm) for transactions of shorter duration.

On the other hand, some TDUs and power marketers support the one-hour minimum term. TAPS argues that transmission providers should not be permitted to restrict the availability of hourly, daily or weekly transmission service at reasonable prices, as some transmission providers have proposed in open access cases. Brazos supports a minimum duration of service equal to the minimum scheduling period of the transmission owner. Turning to the maximum term of service, Chugach objects to the imprecise requirement that transmission service be offered for a term equal to the life of a particular generation resource. Chugach, joined by VEPCO, suggests that the Commission require transmitting utilities to offer five-year terms (with longer contract terms by negotiated agreement).

Although BPA supports eliminating arbitrary term limitations and facilitating long-term resource commitments, it is concerned that the Commission's failure to specify a maximum term for firm transmission service (particularly where no specific resource is being wheeled) requires transmitting utilities to effectively sell off their transmission capacity to third parties. In BPA's view, such a requirement goes well beyond the intent of the Energy Policy Act.

PSE&G argues that the term limit for firm transmission service should be consistent with the transmission provider's planning horizon (e.g., for PSE&G, 10 years), which will ensure comparability of firm third party customers with native load. According to ConEd, failure to specify a maximum term for service creates uncertainty for planning purposes. PECO believes that utilities should have the right to limit the term of service to either: (1) The expected useful life of facilities used in providing service; or (2) the term of permits and land rights needed for those facilities.

Commission Conclusion

We will adopt a one-day minimum term for firm point-to-point service. The one-day minimum term for firm point-to-point service, along with modifications to the procedures for requesting firm point-to-point service, will moot a number of reliability concerns and allegations about possible "cream-skimming." As discussed supra, firm service requests with longer durations of service will have bumping rights over shorter term firm service requests. Also, the one day minimum will not disadvantage anyone because the transmission provider will be subject to the same one-day

term for its firm point-to-point uses of the transmission system. Because of the longer-term nature of network service, it will be subject to a one-year minimum term.

We will not specify a maximum term for either point-to-point or network transmission service. However, we recognize the concerns raised by commenters that a **[31,753]** commitment of uncertain duration makes planning difficult. Therefore, we will modify the tariff to require that an application for transmission service specify the length of service being requested. This will provide the transmission provider with the certainty it needs for planning, and the transmission customer with the flexibility to request the service it needs.

* * * * *

[pp. 31,764 - 31,766]

[31,764]

(a) Transmission Provider's Use of Its System (Charging Yourself)

The purpose of functional unbundling is to separate the transmission component of all new transactions occurring under the Final Rule pro forma tariff, thereby assisting in the verification of a transmission provider's compliance with the comparability requirement. For example, if a transmission provider makes an off-system power sale, functional unbundling requires that the revenues received from that third-party customer be unbundled into specific transmission and production components. The transmission component of the revenues would be the product of the amount of

transmission capacity used in making the sale and the applicable rate. With respect to off-system sales, the transmission provider would book to operating revenue accounts those revenues received from the customer to whom it made the off-system sale. We will require that the transmission service component and energy component of those revenues be recorded in separate subaccounts of Account 447, Sales for Resale.

(b) Facilities and System Impact Studies

Comparability mandates that to the extent a transmission provider charges transmission customers for the costs of performing specific facilities or system impact studies related to a service request, the transmission provider also must separately record the costs associated with specific studies undertaken on behalf of its own native load customers, or, for example, for making an off-system sale. Utilities choosing this method of recovering the cost of specific studies must keep detailed expense records pertaining to each specific study. We will require utilities to record the cost of such studies that are properly includable in the determination of net income for the period in a separate subaccount of Account 566, Miscellaneous Transmission Expenses. We note, however, that not all studies performed by a transmission provider will benefit only a single customer. To the extent a transmission provider performs a system impact study that is useful in providing service to all transmission customers, the costs should be allocated to all customers.

(c) Ancillary Services

To ensure comparable transmission access a transmission provider is obligated to provide, or offer to provide, certain ancillary services to the transmission customer. Also, the transmission provider may offer to provide other ancillary services to the transmission customer, as discussed in Section IV.D. A transmission customer is obligated to purchase certain ancillary services from the transmission provider.

Generation resources provide certain ancillary services, while transmission resources provide other ancillary services. Consequently, the costs of providing certain ancillary services are recorded in the transmission provider's power production expense accounts,[504] while others are recorded in the transmission provider's transmission expense accounts.

Some commenters suggest that there may be a need for revising the Uniform System of Accounts to better track the **[31,765]** costs of providing discrete ancillary services. Other commenters believe that ancillary services are transmission-type services and suggested that the costs of generation-provided ancillary services be refunctionalized from power production expense to transmission expense.

---

[504]This discussion applies to vertically integrated transmission providers. It may not apply, for example, to a transmission-only company or an independent system operator.

Currently, the Uniform System of Accounts requires that costs incurred in providing ancillary services are recorded as power production or transmission expense depending upon which resource the transmission provider uses to supply the service. At this time, we are not convinced that the amounts involved or the difficulty associated with measuring the cost of ancillary services warrants a departure from our present accounting requirements. However, in calculating separate rates for specific ancillary services utilities must maintain sufficient records and cost support for the derivation of the rates. Additionally, we will specify that the revenues a Transmission Provider receives from providing ancillary services must be recorded by type of service in Account 447, Sales for Resale, or Account 456, Other Electric Revenues, as appropriate.

(3) Liability and Indemnification

A number of commenters addressed the liability and indemnification provisions of the proposed pro forma tariffs. Duke argues that the proposed language confuses and conflates the limitation on the Transmission Provider's and Customer's rights against each other if a force majeure event occurs, and the requirement of indemnification against claims by third parties.

EEI argues that the proposed indemnification provision is inappropriate because it applies both ways, that is, the Transmission Provider and Customer indemnify each other against third party claims arising on their own systems. EEI suggests that the provision, as written, could result in the utility being required to indemnify the customer against damages incurred if, for example, an individual pried open a

transformer to steal materials and in the process was electrocuted. This concern was also voiced by Consolidated Edison, NYSEG, and Virginia Electric and Power Company. Consumer Power suggests that the best answer to this issue may be to leave the issue of allocation of risk to the contracting parties, to be resolved by negotiation when a Service Agreement is drawn up.

The Coalition for a Competitive Market, on the other hand, argues that the indemnification provision, as proposed, provides too much of a limitation of the Transmission Provider's liability, requiring gross negligence rather than simple negligence before the Transmission Provider can be held liable for damages to third parties arising from the Transmission Provider's actions.

Commission Conclusion

We agree with the commenters that these risk allocation provisions must be carefully drafted so that transmission providers and customers can accurately assess and account for their respective risks. The indemnification provision has now been broken into two parts. The first part is a force majeure provision which provides that neither the transmission provider nor the customer will be in default if a force majeure event occurs, but also provides that both the transmission provider and customer will take all reasonable steps to comply with the tariff despite the occurrence of a force majeure event. This protection against unexpected and unpredictable events is appropriately made available to both the transmission provider and transmission customer.

The second portion of the provision provides for indemnification against third party claims arising from the performance of obligations under the tariff. We have limited the indemnification portion of the provision so that it is now only the transmission customer who indemnifies the transmission provider from the claims of third parties. The customer is taking service from the transmission provider and may appropriately be asked to bear the risks of third-party suits arising from the provision of service to the customer under the tariff. We find that this new indemnification provision would be too strict if it required customers to indemnify transmission providers even in cases where the transmission provider is negligent. See Pacific Interstate Offshore Company, 62 FERC para. 61,260 at 62,733-34 (requiring amendment of indemnification provisions that required indemnification except in cases of "gross negligence"). Accordingly, the revised provision provides that the customer will not be required to **[31,766]** indemnify the transmission provider in the case of negligence or intentional wrongdoing by the transmission provider.

(4) Miscellaneous Clarifications

(a) Electronic Format

In the NOPR, we proposed that public utilities making Stage Two filings be required, in addition to the requirements specified in Part 35, to file copies of such filings on a diskette in ASCII format. We will now require that public utilities, in addition to complying with the requirements of Part 35, submit a complete electronic version of all transmission tariffs and service agreements in a word processor format, with the diskette labeled as to the format (including version) used,

initially and each time changes are filed. After the initial compliance filing, utilities proposing changes to the Final Rule pro forma tariff terms and conditions must provide a detailed list of changes and, to the extent practicable, provide an electronic version that reflects changes in redline/strikeout format.

* * * * *

[pp. 31,770 - 31,785]

[31,770]

I. Federal and State Jurisdiction: Transmission/Local Distribution In the original Stranded Cost NOPR, the Commission clarified that it has exclusive jurisdiction over unbundled retail transmission in interstate commerce by public utilities: it found that the Commission has exclusive jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, up to the point of local distribution. In the Open Access NOPR, the Commission reaffirmed this jurisdictional determination[515] and also **[31,771]** addressed the distinction

[515]That determination included the situation in which a former bundled retail customer may need unbundled wheeling services from its previous public utility generation supplier, as well as unbundled wheeling from one or more intervening public utilities, in order to reach a distant generation supplier. In that scenario, the Commission would have jurisdiction over all of the transmission facilities used for the unbundled wheeling provided by the intervening public utilities. The NOPR also noted that the Commission would not have jurisdiction over the rates for the sale of generation by the distant supplier because the transaction would

between transmission and local distribution. The Commission stated three reasons for expressing its views on the distinction between Commission-jurisdictional transmission in interstate commerce and state-jurisdictional local distribution, in the context of unbundled retail wheeling by public utilities.[516] First, facilities that can be used for wholesale transmission in interstate commerce by a public utility would be subject to the Commission's open access requirements. Second, states have authority to address retail stranded costs and stranded benefits through their jurisdiction over facilities used in local distribution. Third, as the structure of the industry continues to change dramatically, utilities need to know which regulator has jurisdiction over which facilities and services in order to meet state and federal filing requirements. Accordingly, the NOPR set forth our jurisdictional analysis and several technical factors, for determining what constitutes "facilities used in local distribution."

For unbundled wholesale wheeling, the NOPR proposed to apply a functional test, i.e., whether the entity to whom the power is delivered is a lawful reseller. For unbundled retail wheeling, the NOPR proposed to apply a

be a retail sale. *FERC Statutes and Regulations* ¶32,514 at p. 33,144.

[516]The term "wheeling" is intended to cover any delivery of electric energy from a supplier to a purchaser, i.e., transmission, distribution, and/or local distribution. The Commission also has jurisdiction to order wholesale transmission services in either interstate or intrastate commerce by transmitting utilities that are not also public utilities. *See Tex-La Electric Cooperative of Texas, Inc.*, 67 FERC ¶61,019 (1994), reh'g pending.

combination functional-technical test that would take into account technical characteristics of the facilities used for the wheeling. The Commission proposed seven indicators of local distribution to be evaluated on a case-by-case basis:

(1) Local distribution facilities are normally in close proximity to retail customers.

(2) Local distribution facilities are primarily radial in character.

(3) Power flows into local distribution systems; it rarely, if ever, flows out.

(4) When power enters a local distribution system, it is not reconsigned or transported on to some other market.

(5) Power entering a local distribution system is consumed in a comparatively restricted geographical area.

(6) Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

(7) Local distribution systems will be of reduced voltage.[517]

The NOPR concluded that the application of these tests will enable states to address stranded costs by imposing an exit fee on departing retail customers, or including an adder

---

[517]*FERC Statutes and Regulations* ¶32,514 at p. 33,145.

in the retail customers' local distribution rates.[518] In the NOPR, the Commission also addressed buy-sell transactions in which an end user arranges for the purchase of generation from a third-party supplier and a public utility transmits that energy in interstate commerce and re-sells it as part of a "nominal" bundled retail sale to the end user. We explained that the retail sale is actually the functional equivalent of two unbundled sales (one transmission and the other the sale of power) and that we have exclusive jurisdiction over the voluntary sale by public utilities of unbundled transmission at retail in interstate commerce.[519]

Several commenters support the Commission's proposed jurisdictional demarcation.[520] **[31,772]** San Diego G&E states that the Commission correctly proposed to look at both functional factors (such as whether the service is retail or wholesale) and technical factors (such as voltage). PG&E states that the NOPR's functional/technical test is preferable to a bright line voltage test.

Consumers Power states that the Commission has exclusive jurisdiction over all wheeling on an interconnected interstate transmission grid. It suggests that the Commission and the states act through a joint board or hearing to resolve jurisdictional differences and develop a bright line test.

---

[518]Id. at p. 33,144-45.

[519]As discussed infra, there also would be a component of local distribution in such a transaction that would be subject to state jurisdiction.

[520]*E.g.*, PG&E, Wisconsin Coalition, Com Ed.

PSE&G and PG&E express concern that if retail wheeling is implemented, there may be loopholes that would enable customers to evade state jurisdiction and thus avoid paying stranded costs. For example, PSE&G is concerned that a retail customer may request transmission service only and a state commission will be unable to attach a retail stranded cost surcharge to that customer. PG&E proposes adding another indicator to the functional/technical test -- a final tap to a retail customer -- to ensure that "high-voltage" retail customers do not evade the state's reach. Moreover, to ensure that retail customers cannot escape state jurisdiction, PG&E recommends that the Commission state, as a matter of policy, that "all retail customers taking retail transmission service from their host utility by definition take service over local distribution facilities."

CINergy agrees with the Commission that a distinction between transmission and local distribution is important, but emphasizes the practical need for clarity on a timely basis. To achieve certainty, CINergy proposes that the Commission allow public utilities to file, under section 205, classifications of their facilities as transmission or local distribution. CCEM endorses CINergy's proposal. Although NARUC disagrees that the Commission has jurisdiction over unbundled retail transmission, if the Commission reaffirms the NOPR regarding its jurisdiction, then NARUC supports CINergy's proposal.

PSE&G strongly supports the Commission's proposed case-by-case methodology for determining whether facilities should be classified as transmission or local distribution. SoCal Edison argues that since a utility may have difficulty determining which of its facilities are transmission and which

are local distribution, utilities and states should be able to ask the Commission to classify a particular facility. Portland and Orange & Rockland suggest that the Commission provide a forum to resolve disputes over the correct classification of particular facilities.

Ohio Edison states that the Commission should assume jurisdiction over unbundled retail transmission, but only where a state has required this unbundling. It also believes that the Commission should assert jurisdiction over the ancillary services necessary to provide this jurisdictional service.

NYSEG argues that the Commission lacks jurisdiction over the transmission component of bundled retail service. On the other hand, NYSEG argues that the statute, legislative history, and case law reveal that the Commission has jurisdiction over unbundled retail wheeling from source to load, since it is transmission in interstate commerce. NYSEG argues that the "local distribution" exception to the Commission's jurisdiction applies only to bundled sales of power at retail.

Several state commissions assert that states have rate authority over all facilities used to provide retail service.[521] IL Com argues that states have rate authority over all facilities used to provide retail service, regardless of whether the NOPR would classify these facilities as transmission or local distribution.

---

[521] *E.g.*, NM Com, NC Com, AZ Com.

MI Com, citing Connecticut Light & Power Company v. Federal Power Commission, 324 U.S. 515 (1945) (CL&P), and Arkansas Electric Cooperative v. Arkansas Public Service Commission, 461 U.S. 375, 393-94 (1983), contends that states have plenary jurisdiction over all aspects of retail service, including retail access and unbundled retail transmission service. It asserts that the Commission's effort to expand federal jurisdiction into transmission in connection with retail sales is without statutory justification.

Legal Environmental Assistance argues that the NOPR creates confusion about, and may intrude onto, state jurisdiction. **[31,773]** NYMEX argues that when a state orders retail wheeling, the state should have jurisdiction over that transmission-only service.

Oklahoma G&E, citing CL&P and United States v. California Public Utilities Commission, 345 U.S. 295, 316 (1953), asserts that the Commission failed to explain that the term "transmission in interstate commerce" could have different meanings depending on the factual context in which the term is applied. It argues that "transmission in interstate commerce" means the movement, in bulk, of electric energy flowing in interstate commerce, as opposed to the movement of electric energy that has been subdivided for delivery to consumers.

Oklahoma G&E further argues that "[t]he distinction between interconnected operation and radial operation corresponds precisely to this distinction between activities that have potential interstate effects and those that might have interstate effects but are a matter of primarily local

concern."[522] Oklahoma G&E also disagrees that the transportation of electric energy sold at wholesale necessarily constitutes transmission in interstate commerce. It argues that the Commission has misapplied case precedent and, by focusing on the level of the associated power sale, the Commission has misunderstood what constitutes a functional distinction between transmission in interstate commerce and local distribution.

NY Com asserts that the grant of jurisdiction to the Commission over wholesale power transactions in interstate commerce under section 201 of the FPA does not reduce the states' authority over local distribution (citing CL&P and Federal Power Commission v. Florida Power & Light Company, 404 U.S. 453, 467 (1972)). NY Com argues that the NOPR's assertion of exclusive jurisdiction over all facilities used to deliver electricity for resale, even those traditionally regarded as local distribution, violates Congress' assignment of local electric distribution to the states. It takes issue with the Commission's list of factors and says that states and the Commission should agree on a definition that preserves the traditional classification of local distribution facilities. According to NY Com, such definition should focus on the functional characteristics of local electric systems -- i.e., electricity flows into a comparatively restricted geographic area and does not flow back out of that area, and the power is consumed in that area.

NY IOUs argue that the Commission has jurisdiction over unbundled, but not bundled retail wheeling. It says that

---

[522]Oklahoma G&E Initial Comments at p. 16.

other factors, including the indicators listed in the NOPR, are irrelevant, and that even long-distance interstate transmission is under state jurisdiction as long as it is bundled with a retail sale. According to NY IOUs, this is the plain meaning of the FPA; resort to legislative history is unnecessary. NY IOUs bases this view on section 201(a), which says that federal regulation extends only to matters not subject to state regulation. NY IOUs says that the only matters subject to state regulation were bundled retail sales, and that since transmission was part of the bundle, Congress intended transmission to stay under state authority as long as it is part of that bundle. It also cites section 201(b), which sets forth exceptions from Commission jurisdiction, and section 201(c), which defines "transmission in interstate commerce" and thus also controls the definition of transmission in intrastate commerce. Finally, NY IOUs argues that the legislative history supports its view, as does the case law.

Central Louisiana believes that the costs of requiring a transmission provider to take unbundled transmission service for both wholesale and retail purposes would far exceed any benefits. In this regard, Central Louisiana says that states clearly have jurisdiction over bundled retail transmission charges and that the proposed approach could not be implemented without states giving up jurisdiction or the passage of new federal legislation.

MN DPS disagrees on legal and policy grounds with the Commission's assertion of jurisdiction over unbundled retail transmission services.[523] It maintains that the

---

[523]See also OH Com.

Commission's arguments do not negate the language of the FPA specifying that regulation of retail sales of electric energy is reserved to the states. MN DPS argues that the Commission's arguments **[31,774]** in support of its position are not on point because the issue is state authority to set rates for retail sales, not interstate commerce. Further, it declares that jurisdiction over a service does not change simply because it is priced differently.

Several commenters argue that unbundled pricing should not expand the Commission's jurisdiction.[524] NARUC argues that the NOPR did not explain why the Commission's authority attaches only to unbundled retail transmission service, why unbundling is jurisdictionally significant, and how transmission of electricity to end users differs from unbundled interstate transmission of natural gas by local distribution companies, which is subject to state regulation. Thus, NARUC urges the Commission not to claim jurisdiction over unbundled retail transmission services.

NARUC also argues that the Commission's test for distinguishing between transmission and local distribution is not a bright line as discussed in Federal Power Commission v. Southern California Edison Company, 376 U.S. 205 (1964) (Colton). NARUC concludes that when a state determines to enable a retail customer to purchase power from a third-party provider, that state retains the authority to regulate the delivery service provided by the utility.

---

[524]*E.g.*, DOD, NM Com, KY Com, ABATE.

IL Com asserts that the test should be whether the utility function over which the Commission seeks to exercise jurisdiction is one which falls within the Attleboro gap.[525] It argues that the Commission has no legal authority to prescribe conditions under which a public utility may provide transmission service within its own service territory to its own retail customers. IL Com concedes that the court cases cited by the Commission can be interpreted to support widely disparate legal and policy positions, but argues that those cases resolved questions of Commission jurisdiction in circumstances where wholesale sales of electric power were being examined and not circumstances where retail sales are being considered. It contends that the question of whether the Commission should exercise jurisdiction over all transmission in retail wheeling has never been addressed before and requires a careful examination of the underlying purposes of Congress in enacting the FPA. IL Com explains that transmission by an Illinois utility of power to a retail consumer within its own service territory is not subject to Commission jurisdiction because that transmission was never within the Attleboro gap and has always been regulated by states.

OK Com recommends that the Commission apply to the electric industry the same policy that it has adopted concerning its regulation of the gas industry and leave unbundled retail service regulation to state authorities.

---

[525]*See Public Utilities Commission v. Attleboro Steam & Electric Company*, 273 U.S. 83 (1927).

WI Com argues that if a utility offers unbundled retail access, jurisdiction over transmission services should continue to be based upon the historical demarcation between wholesale and retail transactions. KY Com argues that Congress did not intend, by authorizing wholesale wheeling in the Energy Policy Act, to change the longstanding division of jurisdiction between the Commission and the states. It claims that the NOPR ignores the limitation in the FPA that the Commission has no jurisdiction over retail sales service. NV Com cites several cases noting the states' historical authority to regulate retail rates.

IA Com proposes a definition of local distribution and transmission that would preserve the jurisdictional status quo and does not put a state commission in the position of losing authority over certain elements of a retail transaction should it allow retail wheeling. IA Com's proposed definition is as follows:

> Distribution -- Service provided by a utility directly connected to an ultimate consumer of electricity is a distribution service with respect to electric energy delivered to that consumer.
>
> Transmission -- Service provided by a utility with respect to electric energy to be delivered to an ultimate consumer through another utility is a transmission service.[526]

[31,775]

---

[526]IA Com Initial Comments at p. 4.

Montana Power states that a reasonable way to give effect to the "local distribution" exemption is to define "local distribution" as a bundled retail sale, even if interstate facilities are used.

Several commenters criticized the NOPR's functional/physical indicators. PA Com disagrees with the Commission's discussion of the FPA's legislative history and asserts that the FPA does not address the issue of what constitutes local distribution. PA Com contends that the issue was resolved by the Supreme Court in CL&P in a manner contrary to the Commission's technical-functional test and that the NOPR minimized CL&P. NM Com asserts that the proposed engineering and functional elements for determining the status of local distribution facilities fail to account for the governmental or legalistic test requirement of the FPA as identified in CL&P.

KY Com concludes that a physical definition of distribution facilities, based on objective criteria, is consistent with the FPA and is necessary to provide a clean line of demarcation.

CO Com argues that Congress used a transactional test rather than a functional test and that Congress intended all retail transactions to be under state jurisdiction. According to CO Com, there is concurrent jurisdiction over unbundled transmission in interstate commerce to an end-user. Moreover, CO Com asserts that unbundled intrastate transmission to a wholesale purchaser is under state jurisdiction (citing section 201(b)(1)). Finally, CO Com argues that the state has authority over unbundled transmission in intrastate commerce to an end-user when the

transmission-providing utility, end-user, and generator are all within the same state.

Other commenters prefer a functional test. Natural Resources Defense, DOE, and Sustainable Energy Policy generally agree that a line needs to be drawn between transmission and local distribution but believe that the Commission's test is unnecessarily cumbersome or may lead to legal uncertainty, at least within the context of stranded benefits. Instead, Natural Resources Defense proposes the following functional test, which is based on end-use service:

The Federal Power Act does not affect state regulators' jurisdiction to apply distribution charges -- either volume-based or fixed -- to electricity that is used by any utility customer to provide end-use services (as distinguished from electricity that is purchased for resale to end-use customers).[527] Sustainable Energy Policy endorses Natural Resources Defense's position. DOE suggests that a functional definition of local distribution (i.e., electricity provided for end-use service) may be the best way to avoid legal uncertainty.

EPA argues that the Commission's proposed physical definition may encourage gaming to avoid stranded costs and costs associated with public policy goals such as energy efficiency, renewable energy development and R&D funding, and a physical definition assumes that power flows into, and not out of, distribution systems, which would not allow for distributed generation (e.g., fuel cells). Thus, EPA urges the

---

[527]Natural Resources Defense Initial Comments at p. 3.

Commission to adopt a functional definition that "local distribution occurs whenever electricity is provided by a utility for end-use service." Alternatively, EPA suggests that the Commission add a provision to its approach that "the provision of electricity for end-use service generally involves local distribution." Sustainable Energy Policy suggests a non-bypassable charge levied on all users of the distribution system. It endorses the policy formulation set forth by Natural Resources Defense in its initial comments. Reynolds wants to ensure that there is always at least concurrent state jurisdiction over lines used to serve end-use customers, since only states can order retail wheeling.

Detroit Edison argues that state/federal jurisdictional issues should be resolved by focusing on the use of the facilities. It says that facilities that are used to distribute a utility's own power to its own local customers should be subject to state regulation, while the use of facilities for wholesale power transactions or wholesale or retail transmission in interstate commerce should be under federal regulation.

[31,776]

Mountain States Petroleum Assoc argues that the Commission should use a functional test based on state boundaries: if a line is in more than one state, there is Commission jurisdiction; if a line is entirely within one state, there is state jurisdiction.

MD Com states that it believes that the Commission's proposed indicators for determining where to draw the line are adequate, but adds that it does not concede the

Commission's assertion of jurisdiction over unbundled retail transmission.

Some commenters suggest that implementation of the NOPR's tests could have adverse consequences. NH Com objects to the NOPR's specific tests; for example, if the Commission asserts jurisdiction over facilities because they are not radial, New Hampshire's policy of encouraging looping rather than radial lines would have the ironic effect of destroying state jurisdiction. NJ BPU states that there may be situations when the NOPR factors would not produce the proper result. It requests that the final rule recognize the need for case-by-case flexibility in determining where federal jurisdiction ends, so that the Commission and the states can work cooperatively.

NRRI argues that the NOPR's test could make siting of new transmission lines more difficult because states have in the past required native load customers to pay that part of the transmission-related revenue requirement that is not covered by unbundled transmission service. NRRI contends that, if the Commission asserts jurisdiction over all unbundled transmission service and if there is a firm point-to-point service capacity right that has value and is reassignable, then state commissions might eliminate portions of the transmission systems subject to capacity rights from rate base. NRRI is also concerned that the NOPR's transmission/local distribution test could create a price squeeze between bundled and unbundled retail transmission rates.

IN Com argues that the NOPR's view of jurisdiction would discourage retail wheeling. It says that states will be reluctant to order wheeling if the result is that they lose

jurisdiction over the previously rolled-in transmission aspect of the service. It suggests that the Commission use negotiated rulemaking to address jurisdictional issues.

Several commenters suggest alternative approaches to jurisdictional line-drawing. NV Com suggests that the Commission consider federal and state jurisdiction over transmission by using "network" and "non-network" concepts:

The "network" concept for regulation recognizes that there is an interstate network of electric facilities used to link generation with loads. The operation of that network is indifferent to whether the electrical flows are retail or wholesale flows. Conceptually, events on the network could fall under federal jurisdiction. Where facilities provide essential service for the delivery of power, but do not substantially affect the electrical flows on the network, the facilities fall outside the network and would remain within the traditional domain of the state commission. As a consequence the delineation of federal and state jurisdiction evolves from the recognition of the events and where they occur as opposed to a rigid consideration of the physical properties of the facilities involved.[528]

NV Com further explains that the determination of what is a network event would require a case-by-case examination.

OH Com asserts that Congress intends there to be a bright line between state and federal jurisdiction and that the Commission has failed to provide such a bright line. OH Com

[528]NV Com Reply Comments at p. 3.

proposes the use of retail marketing areas to provide the bright line -- the jurisdictional line would be at the point at which power enters the retail marketing area of the entity delivering the power to the retail customer. OH Com cites section 212(g) of the FPA, as amended by the Energy Policy Act, which provides that the Commission cannot issue any order under the FPA inconsistent with state law governing retail marketing areas.

Under OH Com's proposal, the Commission would have jurisdiction over the wheeling-out and wheeling-through components of retail wheeling and the state would have jurisdiction over the wheeling-in component due to its local nature. OH Com concludes that the Commission's approach "fails to meet the legal standard **[31,777]** FERC must consider, and is inconsistent with the 'savings clause' and legitimacy of 'retail marketing areas' as discussed in the amended FPA."[529] OH Com also explains that the Commission's approach "is wreaking havoc on the state's ability to develop an interruptible buy-through arrangement to provide an increased competitive option for its retail customers."[530] OH Com further encourages the use of mutual

[529]Sections 212(g) and 212(h) of the FPA.

[530]We note that since OH Com filed its comments, it approved an interruptible buy-through plan. *See Interruptible Electric Service Guidelines*, Case No. 95-866-EL-UNC, --PUR 4th-- (Ohio PUC Feb. 15, 1996). *See also Central Illinois Light Company*, Docket No. ER96-1075-000 (1996) (accepting amendment to open access transmission tariffs that expands service eligibility to accommodate participation in experimental retail wheeling pilot program approved by the Illinois Commerce

deference to promote Congress' intent in mandating a system of federal/state cooperation. In support, OH Com cites federal and state enforcement of telecommunications laws. NRRI also suggests that the jurisdictional line be drawn at the retail marketing area.

DC Com argues that the NOPR test is too difficult to administer and will create problems in determining the rate base at the state level. It suggests that the Commission should have jurisdiction over transmission from the source to the boundary of the "home" utility that delivers the power to the customer, with state jurisdiction over all aspects of the transmission service within that utility's franchise territory. AZ Com also expresses doubts that the NOPR's test is workable.

Several commenters propose that the Commission and state authorities address the jurisdictional issue jointly. SBA characterizes the Commission's proposed demarcation line as "laudable but misguided."[531] SBA recommends that a federal/state board be established to resolve the transmission/local distribution dilemma, similar to what

---

Commission); *Illinois Power Company*, Docket No. ER96-1285-000, 75 FERC (1996); *cf. Illinois Power Company*, --PUR4th--, No. 95-0494 (Illinois Commerce Commission Mar. 13, 1996) (offering retail direct access service providing transmission and ancillary services using the rates, terms, and conditions of Illinois Power's open access tariff on file with the Commission); recently introduced legislation in Rhode Island, H.B. 8124, the Utility Restructuring Act of 1996.

[531]SBA Initial Comments at p. 36.

Congress did for allocating costs between interstate and intrastate communications. SBA explains that the problem in the communications industry was the impossibility of allocating a portion of a single copper wire to interstate or intrastate service.

AZ Com notes that even if the Commission is correct, the FPA clearly does not preempt a state from concluding that retail transmission or other direct access programs should be implemented in that state. AZ Com suggests that there may be concurrent jurisdiction and that mutually agreed-upon principles should be implemented to determine which jurisdiction should be given deference.

MD Com states that in determining the status of particular facilities, the Commission should give substantial weight to determinations made by states. ABATE states that the Commission could initially defer to states with respect to the determination of rates, terms, and conditions, while maintaining the right to review and overturn the state determination.

If the Commission maintains its position concerning jurisdiction, NARUC argues that the Commission should not implement its multi-factor test, but should enter into discussions with state commissions to develop workable alternatives. NH Com argues that pricing the retail part of a transaction, even if it involves use of the transmission system, should be subject only to state jurisdiction. NH Com wants to create a mechanism by which state and federal regulators combine their efforts in cooperative regulation; it suggests several alternatives such as state/federal agreements for shared jurisdiction.

KY Com and NRRI object to the statement in the NOPR that retail buy-through service is really transmission service (subject to the Commission's jurisdiction) plus a sale of generation at retail (subject to state jurisdiction). From a policy standpoint, KY Com argues that the Commission's approach creates a powerful disincentive for a state to embark on changes that otherwise might foster a more competitive environment. NRRI argues **[31,778]** that the Commission's approach may violate sections 212(g) and 212(h).

IL Com is concerned that industrial customers who get direct access may attempt to evade state jurisdiction, and thus avoid retail stranded cost charges, by bypassing facilities such as radial lines. It contends that retail wheeling rate surcharges would be a more effective means of recovering retail stranded costs if states were allowed to apply them to unbundled transmission and local distribution rates, not just the local distribution component of such rates.

NC Com asserts that "[a] significant cottage industry may well arise solely to convert retail customers into wholesale customers, thereby subverting the intent of Congress as expressly set forth in EPACT."[532] If the Commission does not adopt NARUC's proposal, NARUC asserts that the Commission's functional test should not permit an end user to bypass the distribution service provided by the utility. It urges the Commission to assure that there will be some facility involved in the transaction that will be defined as providing a local distribution service.

---

[532]NC Com Initial Comments at p. 7.

NARUC also requests that the following sentence be added to proposed 18 CFR 35.27:

Nothing in this part limits the authority of a State commission in accordance with State law (1) to allow or disallow the inclusion of the costs of electric energy purchased at wholesale in retail rates subject to such State commission's jurisdiction, (2) to establish competitive procedures for the acquisition of such electric energy, or (3) to establish non-discriminatory fees for the delivery of such electric energy to retail consumers for purposes established in accordance with State law.([533])

Duke is concerned about the potential for regulatory gaps, which could lead to costs not being recovered from either federal or state jurisdiction. Duke is also concerned that where facilities are used for both wholesale and retail transactions, costs might not be recovered if federal and state regulators use different methods of cost allocation.

In response to the NOPR's proposal for functional unbundling,[534] CA Com agrees that it is important to draw a distinction between transmission and local distribution and that a bright line is not possible, but suggests that corporate or functional unbundling might provide a means to establish a workable bright line without relying on the more qualitative approach proposed in the NOPR. Arizona argues that rather than unbundling transmission for retail purposes, each utility

---

[533]NARUC Reply Comments at p. 15-16.

[534]*FERC Statutes and Regulations* ¶32,514 at p. 33,080-83.

should establish a distribution function that would obtain transmission on behalf of retail customers, taking service under the utility's tariff. Arizona states that this would simplify the allocation of transmission costs, since all transmission costs would be under the Commission's jurisdiction. Arizona argues that the Commission should permit the utility to recover the distribution rate approved by the state. According to Arizona, this would create a bright line between state and federal jurisdiction.

TX Com argues that the proposed test would not be applicable to intrastate utilities in Texas because they do not operate in interstate commerce. Thus, it asserts that it should continue to regulate Electric Reliability Council of Texas (ERCOT) transmission and distribution service and deal with stranded cost issues that arise in connection with any retail wheeling initiatives.

Several commenters object to the Commission's proposal to assert jurisdiction over transactions that are buy-sell transactions in name only.[535] AEP argues that the Commission should avoid an unnecessary conflict over state/federal jurisdiction that may be caused by the NOPR's statement that buy-sell transactions are in fact transmission subject to Commission jurisdiction. It suggests that the Commission attempt to reach agreement with the states on this matter or ask Congress for any necessary statutory change. Citizens Utilities also argues that the Commission should not unbundle the interstate transmission aspect of buy-sell transactions. It says that, unlike the analogous **[31,779]** gas

[535]See id. at p. 33,082.

contracts, buy-sell arrangements on the electric side are not an end run around clear federal jurisdiction. Further, it argues that it would be very difficult to define those buy-sell transactions that truly belong under federal jurisdiction.

IL Com also objects to the NOPR's characterization of buy-sell transactions. It argues that the fact that a transaction becomes unbundled does not suddenly make part of it under federal jurisdiction. Nucor argues that there is no need for the Commission to resolve this issue now; it suggests that the buy-sell arrangement is only tangentially related to open access. It argues that each buy-sell transaction will have to be addressed individually.

UT Com seeks clarification as to what the Commission means by buy-sell arrangements:

> we currently authorize interruptible "buy-through" contracts, through which a retail customer, taking service subject to interruption for either economic or technical reasons, can opt to "buy-through" an interruption. The public utility purchases energy on behalf of the customer and sells it at cost to the customer. In our opinion, such transactions are not an example of a buy-sell transaction within the meaning of the proposed rule.[536]

DOD objects to the statement in the NOPR that "buy-sell" transactions are not really bundled retail service. It says that this view will discourage the development of innovative state programs, such as direct access programs. NYSEG also

[536]UT Com Initial Comments at p. 4-5.

argues that buy-sell transactions are not under the Commission's jurisdiction. It argues that these transactions are unlike buy-sell transactions on the gas side, where the Commission asserted jurisdiction to prevent LDCs from circumventing the nondiscrimination standard it imposed on the release of capacity. NYSEG says:

> In contrast to its regulation of gas buy-sells, if the Commission regulates electric buy-sell transactions it would forego regulation of a transaction in which the Commission has a significant interest (i.e., access to the upstream seller's transmission), to regulate a transaction in which the Commission has virtually no interest (i.e., access to the distributing utility's system). Electric utilities must serve each retail customer irrespective of whether the customer takes traditional bundled service or retail buy-sell service. Unlike excess upstream gas pipeline capacity, the capacity on the local utility's electric system would not be allocated to another customer in a FERC jurisdictional transaction absent the electric buy-sell transaction. Electric buy-sell transactions are not designed so as to manipulate the assignment of upstream transmission capacity. Consequently, the impetus for FERC to reclassify gas buy-sell transactions as capacity assignments is not present in the electric context.[537]

NYSEG argues that there are only two possible grounds for the Commission's assertion of jurisdiction over electric buy-sell transactions: either (1) the sale for resale by the supplier is really a sale at retail to the end user, and the resale by the local utility is really unbundled retail wheeling;

[537]NYSEG Initial Comments at p. 48 (footnote omitted).

or (2) the Commission has jurisdiction over transmission service that is part of bundled retail service. It claims that the second ground is invalid because the transmission aspect of bundled retail service is distribution. It also claims that the first ground is invalid because it assumes that the sale by the supplier to the local utility is not a sale for resale even though the contract says that it is. NYSEG states:

> The logical outcome would be that FERC would not have jurisdiction over the sale by the supplier to the utility, including transmission by that supplier because it would be a bundled retail sale. This is because, if the commission holds the resale to be a retail wheel, then it would have to find that the sale by the supplier is a retail sale to the end user. The Commission cannot at once regulate the sale for resale and the "retail transmission service." The Commission would regulate the transmission rates of the local franchise utility, although it would not regulate the access to such transmission service -- a matter FERC leaves to state regulators. In the process, FERC **[31,780]** would abandon the ability to regulate access to the supplier's bundled "retail power sale and transmission service," a transaction that FERC arguably has an interest in regulating.[538]

Finally, NYSEG argues that if the Commission insists on asserting jurisdiction, it should at least grandfather existing contracts.

UT Industrials state that where there is a state barrier to a buy-sell transaction, the Commission should allow the

[538]NYSEG Initial Comments at p. 50.

utility to file a tariff with the Commission that would permit the utility to complete a voluntary buy-sell transaction as the NOPR proposes. However, it contends that when a state regulatory authority is authorized to, and has approved buy-sell transactions, it is not necessary for the Commission to become involved. It urges the Commission to allow such transactions to take place free of Commission regulation.
Commission Conclusion

In the discussion below, the Commission addresses the following jurisdictional issues raised in the prior NOPRs:

a. Does the Commission have jurisdiction over unbundled transmission in interstate commerce by a public utility when such transmission is used to transport electric energy that is sold to an end user?

b. If so, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to an end user?

c. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to a purchaser who will then re-sell the energy to an end user?

d. What procedures are appropriate for making jurisdictional determinations?

In addition, the Commission addresses concerns raised by state regulators which indicate that competition and open

access are perceived as threatening the traditional regulatory functions of state commissions. The Federal Power Act differentiates between state and federal regulation of electric power. As we discuss below, the Commission believes that any change in state or federal jurisdiction over physical transmission assets and related costs will not affect the traditional tasks of state and federal regulators.

The wide range of jurisdictional interpretations and proposals in the comments reflects the fact that the legislative history of the FPA and case law interpreting federal/state jurisdiction under that Act and the Natural Gas Act grew out of a market structure in which electricity and transmission generally were bought and sold on a bundled basis. As a result, most transactions included either a retail or wholesale sale of electric energy and jurisdictional lines were drawn on the basis of this sale. Thus, the cases simply do not resolve dispositively these jurisdictional issues when they arise in the context of the market structures and unbundled transactions being contemplated in today's electric industry. However, after reviewing the extensive analysis of the FPA, legislative history, and case law contained in both our initial Stranded Cost NOPR and in our Open Access NOPR, and the comments received on that analysis, we continue to believe that we were correct in asserting jurisdiction over the transmission component of an unbundled interstate retail wheeling transaction. We therefore reaffirm our conclusion. We also reaffirm and clarify our determinations regarding the tests to be used to determine what constitute Commission-jurisdictional transmission facilities and what constitute state-jurisdictional local distribution facilities in situations involving

unbundled wholesale wheeling and unbundled retail wheeling.[539]

At the same time, the Commission strongly supports the efforts of states to pursue pro-competitive policies. We recognize that jurisdictional issues raise overlapping Federal and state policy concerns that call for heightened cooperation among federal and state regulators. As discussed below, where states unbundle **[31,781]** retail sales, we will give deference to their determinations as to which facilities are transmission and which are local distribution, provided that the states, in making such determinations, apply the seven criteria discussed in the NOPR and reaffirmed below. In addition, we clarify our view that there is an element of local distribution service in any unbundled retail transaction, and further clarify other aspects of our jurisdictional ruling to preserve state jurisdiction over matters that are of local concern and will remain subject to state jurisdiction if retail unbundling occurs.

We first address our legal determination that if unbundled retail transmission in interstate commerce occurs voluntarily by a public utility or as a result of a state retail access program, this Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission. No commenter has raised cases or legislative history not previously considered in our prior NOPRs, and we will not

---

[539]Not only do we conclude that our determinations are legally supportable under the case law, but we believe it is imperative to provide guidance to public utilities and state regulators as to our position on where the jurisdictional boundaries lie.

repeat here our full legal analysis of this issue.[540] However, we find compelling the fact that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.[541] Unlike our jurisdiction over sales of electric energy, which section 201 of the FPA specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission.

In response to those commenters (including NARUC) who argue that the Commission did not explain why its authority attaches only to unbundled, but not bundled, retail transmission in interstate commerce by public utilities, we believe that when transmission is sold at retail as part and parcel of the delivered product called electric energy, the transaction is a sale of electric energy at retail. Under the FPA, the Commission's jurisdiction over sales of electric energy extends only to wholesale sales. However, when a retail transaction is broken into two products that are sold

---

[540]The Commission's complete legal analysis on this issue, and on the related issue of what facilities are Commission-jurisdictional transmission facilities, and what are state jurisdictional local distribution facilities, are contained in Appendix G to this Rule.

[541]Section 201(b)(1) specifically exempts from Commission jurisdiction facilities used for transmission in intrastate commerce and transmission of electric energy consumed wholly by the transmitter. As a result, we have no jurisdiction over retail wheeling that occurs in Alaska, Hawaii and the Electric Reliability Council (ERCOT) portion of Texas since transactions in those areas are intrastate.

separately (perhaps by two different suppliers: an electric energy supplier and a transmission supplier), we believe the jurisdictional lines change. In this situation, the state clearly retains jurisdiction over the sale of the power. However, the unbundled transmission service involves only the provision of "transmission in interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission. Therefore, when a bundled retail sale is unbundled and becomes separate transmission and power sales transactions, the resulting transmission transaction falls within the Federal sphere of regulation.

In asserting jurisdiction over unbundled retail transmission in interstate commerce by public utilities, the Commission in no way is asserting jurisdiction to order retail transmission directly to an ultimate consumer. Section 212(h) of the FPA clearly prohibits us from doing so. In addition, as stated in both the initial Stranded Cost NOPR and the Open Access NOPR, we do not address whether states have authority to order retail wheeling in interstate commerce. The Commission's assertion of jurisdiction is that if retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

The Commission clarifies that nothing in this jurisdictional determination changes historical state franchise areas or interferes with state laws governing retail marketing areas of electric utilities. Section 212(g) of the FPA prohibits Commission orders that would be inconsistent with such laws.

However, we reject arguments made by some of the commenters **[31,782]** that section 212(g) could somehow be construed to give states authority over the rates, terms, and conditions of unbundled interstate transmission within retail marketing areas.[542] While our jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusivejurisdiction over transmission in interstate commerce by public utilities.

In response to several of the commenters, we further clarify that the Commission's jurisdiction over the rates, terms, and conditions of unbundled retail transmission is no broader than our authority over transmission used for wholesale transactions, and will not affect matters otherwise

---

[542]The legislative history of FPA section 212(g) and its predecessor, former section 211(c)(3), indicates that the provision was focused on not interfering with state laws governing retail service territories and not permitting Commission wheeling orders "for purposes of sale by a utility to an ultimate consumer who is within the service territory of another utility (other than the applicant) where such territory is established by or under State law, rule, or decision." See H.R. Conf. Rep. No. 1750, 95th Cong., 2d Sess. 92 (1978), reprinted in 1978 U.S. Code Cong. & Ad. News 7797, 7826. Nothing on the face of section 212(g) or the legislative history of either the Energy Policy Act or PURPA indicates that the provision in any way affects the Commission's authority over rates, terms, and conditions of transmission in interstate commerce by public utilities.

left to the states by Congress.[543] The Federal Power Act recognizes that retail marketing areas are governed by state law. Moreover, we believe that states have authority over the service of delivering electric energy to end users. In exercising this authority, state regulatory commissions and state legislatures have traditionally developed social and environmental programs suited to the circumstances of their states. State regulation of most power production and virtually all distribution and consumption of electric energy is clearly distinguishable from this Commission's responsibility to ensure open and non-discriminatory interstate transmission service. Nothing adopted by the Commission today, including its interpretation of its authority over retail transmission or how the separate distribution and transmission functions and assets are discerned when retail service is unbundled, is inconsistent with traditional state regulatory authority in this area.

The Commission reiterates its strong interest in preventing any balkanization of the interstate power market. Although the Commission believes its Final Rule will accommodate retail competition, if it is offered voluntarily by a utility or ordered by a state, our policies relate only to the bulk power market and not traditional state regulation of the retail market.[544]

---

[543]Among other things, Congress left to the States authority to regulate generation and transmission siting. See FPA sections 201(b) and 211(d)(1); Section 731 of the Energy Policy Act.

[544]This Final Rule will not affect or encroach upon state authority in such traditional areas as the authority over local service issues, including reliability of local service; administration of

NARUC has requested that the Commission specifically clarify in §35.27 of its proposed rules[545] that nothing in our final rule limits the authority of a state commission "to allow or disallow the inclusion of the costs of electric energy purchased at wholesale in retail rates subject to such State commission jurisdiction." We will adopt NARUC's proposal with modification, but add it as a separate subsection. The Final Rule adopts a new §35.27(b) as follows:

Nothing in this part (i) shall be construed as preempting or affecting any jurisdiction a state commission or other state authority mayhave under applicable state and federal law, or (ii) limits the authority of a state commission in accordance with state and federal law to establish (a) competitive procedures for the **[31,783]** acquisition of electric energy, including demand-side management, purchased at wholesale, or (b) non-discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

---

integrated resource planning and utility buy-side and demand-side decisions, including DSM; authority over utility generation and resource portfolios; and authority to impose non-bypassable distribution or retail stranded cost charges.

[545]Section 35.27 of the proposed rules provided that any public utility seeking authorization to engage in sales for resale at market-based rates shall not be required to demonstrate any lack of market power in generation with respect to sales from capacity first placed in service on or after 30 days from the date of publication of the Final Rule in the Federal Register. *FERC Statutes and Regulations* ¶32,514 at p. 33,154.

With respect to the Commission's adoption of the Open Access NOPR's functional/technical tests for determining what facilities are Commission-jurisdictional facilities used for transmission in interstate commerce and what facilities are state-jurisdictional local distribution facilities, the case law supports a bright line for unbundled wholesale transmission, i.e., transmission of electric energy that is being sold for resale. This is consistent with the bright line drawn by Congress to fill the Attleboro gap for regulating wholesale sales of electric energy. The case law also supports a bright line with respect to retail transmission by intervening utilities, i.e., transmission by those utilities between the new retail generation supplier and the public utility that previously provided bundled retail service to the end user. However, despite many commenters' arguments to the contrary, we cannot divine such a bright line for unbundled retail transmission by the public utility that previously provided bundled retail service to the end user. In fact, the limited case law, including CL&P and Colton, supports a case-by-case determination.[546] Accordingly, we believe our technical test, with its seven indicators, will permit reasoned factual determinations in individual cases.

Although we are unable to draw the bright line for local distribution facilities that many commenters would like, we believe it is important to make two clarifications regarding local distribution in the context of retail wheeling. First, even

---

[546]As noted, the Commission's detailed legal analysis is contained in Appendix G. We are particularly persuaded by the Supreme Court's statement that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. See CL&P, 515 U.S. at p. 534-35.

when our technical test for local distribution facilities identifies no local distribution facilities for a specific transaction, we believe that states have authority over the service of delivering electric energy to end users. Second, through their jurisdiction over retail delivery services, states have authority not only to assess stranded costs but also to assess charges for stranded benefits, such as low-income assistance and demand-side management. Because their authority is over services, not just the facilities, states can assign stranded costs and benefits based on usage (kWh), demand (kW), or any combination or method they find appropriate. They do not have to assign them to specific facilities.[547]

Thus, while we believe in most cases there will be identifiable local distribution facilities subject to state jurisdiction, we also believe that even where there are no identifiable local distribution facilities, states nevertheless have jurisdiction in all circumstances over the service of delivering energy to end users. Under this interpretation of state/federal jurisdiction, customers have no incentive to structure a purchase so as to avoid using identifiable local distribution facilities in order to bypass state jurisdiction and thus avoid being assessed charges for stranded costs and benefits.

Based on concerns raised by state commissions as well as some utilities, we have further determined that it is

---

[547]As noted above, states retain authority over state integrated resource planning, utility resource portfolios, and utility buy-side and demand-side decisions.

appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs. We also believe it is important to develop mechanisms to avoid regulatory conflict and to help provide certainty to utilities as to which regulator has jurisdiction over which facilities. These are discussed below.

Determining where to draw the jurisdictional line for facilities used in unbundled retail wheeling transactions will involve case-specific determinations that evaluate the seven local distribution indicators that we are adopting. We believe that the Commission should take advantage of state regulatory authorities' knowledge and expertise concerning the facilities of the utilities that they regulate. Therefore, in instances of unbundled retail wheeling that occurs as a result of a **[31,784]** state retail access program, we will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[548] Moreover, we recognize that in some cases the Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by states that take into account other

[548]In order to give such deference, we expect state regulators to specifically evaluate the seven indicators and any other relevant facts and to make recommendations consistent with the essential elements of the Rule.

technical factors that the state believes are appropriate in light of historical uses of particular facilities.

Some commenters have asked the Commission to provide a forum to prevent or resolve disputes over the correct classification of facilities as transmission or local distribution. As a means of facilitating jurisdictional line-drawing, we will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the principles established in the Final Rule, the Commission will defer to such classifications and/or cost allocations.[549] We encourage public utilities and their state regulatory authorities to attempt to agree to utility-specific classifications and allocations that the utility may file at the Commission.

A number of commenters have asked the Commission to defer to state commission recommendations or decisions regarding rates, terms and conditions of unbundled retail transmission in interstate commerce by public utilities. Some have suggested that we set broad guidelines for such rates, terms, and conditions, and then allow states to actually

[549]This should also alleviate some concerns about the potential for costs not being accounted for if the Commission and a state commission use different methods of allocating costs.

implement the guidelines. While the Commission cannot simply turn over its jurisdiction for the states to implement, we understand the concerns raised by many state regulators and believe that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances, as discussed below.

As we determined in the NOPR, when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes -- a transmission component and a local distribution component. The Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component.[550] Thus, the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. When this occurs, we will generally expect unbundled retail wheeling customers to take service under the same FERC tariff that applies to wholesale customers. However, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a separate retail transmission tariff[551] to accommodate the design and special needs of such programs. In such situations, the Commission will defer to state requests for

---

[550]As discussed above, even if there were instances where no local distribution facilities are used, we believe states have authority over the service of delivering electric energy to end users.

[551]*I.e.*, the tariff would be different from the tariff that applies to wholesale customers. Such tariff would still be filed with the Commission under FPA section 205.

variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by this Final Rule. In addition, rates must be consistent with our Transmission Pricing **[31,785]** Policy Statement, and the guidance herein concerning ancillary services.[552]

A final jurisdictional issue raised in the Open Access NOPR concerns buy-sell transactions. We remain concerned, just as we were with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, we reaffirm our conclusion that we have jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. However, we recognize that there is a wide range of programs and transactions that might or might not fall within this category. We will address these on a case-by-case basis.

In summary, the Commission reaffirms and clarifies its prior jurisdictional conclusions and tests for determining the demarcation between federal and state jurisdiction over transmission in interstate commerce and local distribution. We have attempted to address these issues in a way that provides

---

[552]In applying the principles of the Final Rule to retail transmission tariffs, the Commission clearly cannot order retail wheeling directly to an ultimate consumer. See FPA section 212(h).

for flexibility and recognition of legitimate state concerns. With regard to retail services, we recognize the states' concerns that the unbundling of retail transactions would result in changes from what historically has been regulated by the states (principally, the rates of transmission assets previously included in retail rate base). However, the decision to provide unbundled retail wheeling is not the Commission's to make because we have no authority to order transmission directly to an ultimate consumer. In addition, even if a retail access program occurs, we do not believe the unbundling of retail transactions will radically change fundamental state authorities, including authority to regulate the vast majority of generation asset costs, the siting and maintenance of generation facilities and transmission lines, and decisions regarding retail service territories. Further, the Commission intends to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies. As the electric industry and state regulatory authorities continue to develop new competitive market structures and consider retail wheeling programs, we believe that the tests and mechanisms we have provided in this Rule will accommodate both Federal and state interests and will help provide jurisdictional certainty to market participants.

* * * * *

[pp. 31,898 - 31,899]

[31,898]

1. Public Utilities

As with the Open Access Final Rule, there are not a substantial number of public utilities that qualify under the SBA's definition of small electric utility that are subject to the Stranded Cost Final Rule. The Stranded Cost Rule applies only to public utilities that seek stranded cost recovery in connection with a limited set of wholesale requirements contracts (those executed on or before July 11, 1994 that do not contain an exit fee or other explicit stranded cost provision). To the extent that public utilities seek stranded cost recovery, they will do so in a rate filing, where stranded cost recovery is likely to be one of many items considered. Accordingly, the Stranded Cost Final Rule will not pose a significant economic impact on a substantial number of public utility small entities.

2. Non-Public Utilities

With regard to non-public utilities, the stranded cost issue would only arise in a proceeding under sections 211 and 212 of the FPA when, in directing transmission, the Commission addresses the stranded cost issue in determining a just and reasonable rate. As with public utilities, stranded costs will be just one more item to be considered in establishing just and reasonable rates for transmission. As a result, the Stranded Cost Final Rule will not impose a significant economic impact on a substantial number of non-public utility small entities.

C. *Conclusion*

Accordingly, the Commission certifies that these final rules will not have a significant economic impact on a substantial number of small entities.

VII. Information Collection Statement

The Office of Management and Budget's (OMB) regulations[1082] require that OMB approve certain information and recordkeeping requirements (collections of information) imposed by an agency. Upon approval of a collection of information, OMB shall assign an OMB control number and an expiration date. Respondents subject to the filing requirements of this Rule shall not be penalized for failing to respond to this collection of information unless the collection of information displays a valid OMB control number.

There are now approximately 328 public utilities, including marketers and wholesale generation entities. The Commission estimates that 166 of these utilities own, control or operate facilities used for the transmission of electric energy in interstate commerce and would be subject to the filing requirements of this Rule.

Title: FERC-516, Electric Rate Schedule Filings

Action: Final Rule

OMB Control No: 1902-0096

[1082]5 CFR 1320.11.

Respondents: Public Utilities that own, control or operate facilities used for the transmission of electric energy in interstate commerce.

Frequency of Responses: On occasion.

Necessity of information: The Final Rule requires public utilities that own, control or operate facilities used for the transmission of electric energy in interstate commerce to have on file with the Commission non-discriminatory open access transmission tariffs that contain minimum terms and conditions of service and permits public utilities to make filings to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and FPA section 211 transmission services. The Commission has a mandate under sections 205 and 206 of the FPA to ensure, with respect to any transmission in interstate commerce or any sale of electric energy for resale in interstate commerce by a public utility, that no entity is subject to undue discrimination. The Commission will use the data collected in this collection of information to carry out its responsibilities under Part II of the FPA. The Commission's Office of Electric Power Regulation will use the data to review electric rate and tariff filings.

The Commission is submitting notification of this Final Rule to OMB. Interested persons may obtain information on the reporting requirements by contacting the Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. **[31,899]** 20426 [Attention: Michael Miller, Information Services Division, (202) 208-1415], and to the Office of Management and Budget [Attention: Desk

Officer for the Federal Energy Regulatory Commission, (202) 395-3087].

VIII. Effective Date

This Rule will take effect on [insert date 60 days after date of publication in the Federal Register]. The Commission has determined, with the concurrence of the Administrator of the Office of Information and Regulatory Affairs of the Office of Management and Budget, that this Rule is a "major rule" within the meaning of section 351 of the Small Business Regulatory Enforcement Act of 1996.[1083] The Rule will be submitted to both Houses of Congress and the Comptroller General prior to its publication in the Federal Register.

List of Subjects

18 CFR Part 35

Electric power rates, Electric utilities, Reporting and recordkeeping requirements.

18 CFR Part 385

Administrative practice and procedure, Electric power, Penalties, Pipelines, Reporting and recordkeeping requirements.

By the Commission. Commissioner Hoecker concurred in part and dissented in part with a separate statement

---

[1083]5 U.S.C. 804(2).

attached. Commissioner Massey dissented in part with a separate statement attached. Lois D. Cashell, Secretary.

* * * * *

[pp. 31,919 - 31,926]

[31,919]

Appendix C--Allegations of Public Utilities Exercising Transmission Dominance

I. Examples From Proceedings Before Administrative Law Judges

These are examples of allegations that various public utilities have refused to provide comparable service, either through refusals to wheel, dilatory tactics that so protracted negotiations as to effectively deny wheeling, refusals to provide service priority equal to native load, or refusals to provide service flexibility equivalent to the utility's own use.

A. *American Electric Power Service Corp. (AEP)*

In 1993, AEP filed, on behalf of its public utility associate companies, an open access tariff that offered only firm point-to-point service with very limited flexibility. It did not offer network service, flexible point-to-point service, or non-firm service. Thus, it did not provide customers with the same flexibility that AEP itself has. Nor did it provide a service priority equivalent to that enjoyed by native load. The Commission set AEP's tariff for hearing and, on rehearing, held that in order not to be unduly discriminatory, the tariff had to offer comparable service. American Electric **[31,920]**

Power Service Corp., 64 FERC para. 61,279 (1993), reh'g, 67 FERC para. 61,168 (1994).

At hearing, Raj Rao of Indiana Michigan Power Agency (IMPA) (Ex. IMPA-1, Feb 23, 1994) and Kenneth Hegemann of American Municipal Power-Ohio, Inc. (AMP-Ohio) (Ex. AMPO-1, Feb 23, 1994), both senior management officials, testified concerning AEP's alleged discriminatory practices.[1] AMP-Ohio is an association of municipalities in Ohio, some of whose members depend on AEP for transmission and partial requirements service. IMPA is an association of municipalities in Indiana, and many of IMPA's loads are captive to the AEP transmission system. The witnesses alleged as follows:

1. In anticipation of high peak demands, AEP would contract for large blocks of available short-term power, withhold sale of short-term power, refuse to transmit third party short-term power, and require purchases from AEP at the emergency rate (100 mill/kwh) when an emergency might not exist. Ex. AMPO-1 at 6.

2. In December 1989, AMP-Ohio negotiated a 20 MW purchase of short-term power from Louisville Gas & Electric Company (LG&E). AEP refused to wheel because LG&E had earlier that day told AEP it had no power to sell to AEP. AEP

[1]After the Rehearing Order expanding the scope of the proceeding, AMP-Ohio and IMPA withdrew this testimony as no longer necessary. This withdrawal does not change the fact that the testimony was sworn to under oath.

then bought the power from LG&E and offered to resell it to AMP-Ohio. Ex. AMPO-1 at 6-7.

3. In January 1990, AMP-Ohio solicited bids for February power purchases from a number of utilities including AEP. AEP was not the winning bid. AMP-Ohio made arrangements to purchase the power from four winning bidders and sought transmission through AEP. When AMP-Ohio gave AEP the schedule for delivery, AEP refused to transmit the power, matched the average price of the winning bids, and made the sale itself. Ex. AMPO-1 at 7.

4. In August 1993, an AMP-Ohio member (Columbus, Ohio) was purchasing 10 MW of hourly non-displacement power from AEP and, after AEP raised its price to 60 mills/kwh, sought another source for the next hour. Consumers Power Company and Detroit Edison Company both offered non-displacement power at 40 mills. AEP refused to transmit, saying it had a 600 MW unit out and could not resell power from another source.[2] Columbus cancelled the transaction and had to buy 10 MW of power from AEP at 100 mills/kwh. Ex. AMPO-1 at 7-8.

5. In July 1993, two AMP-Ohio members (Columbus and St. Mary's) had been buying hourly non-displacement

[2]AEP generally limited its offer of short-term transmission to buy/sell transactions; that is, AEP would buy the power from the seller and resell it to the purchaser. Supplemental testimony of AEP Witness Baker (Ex. A-73) at 27-29. Often, the terms of the buy/sell transaction required transmission dependent utilities (TDUs) to maintain reserves and meet contractual commitments for at least a year. *Id.*

power from AEP when the price rose to 35 mills. Dayton Power & Light Company (DP&L) offered to sell at 23 mills and AEP agreed to transmit for one hour. But for the next hour, AEP said it had problems with its system, refused to transmit the power, kept the power from DP&L for itself and offered to sell power to AMP-Ohio for Columbus and St. Mary's at 100 mills. Columbus increased its local generation, but St. Mary's purchased 8 MW at 100 mills. For the next hour, AMP-Ohio arranged with DP&L for another 8 MW, hoping AEP would transmit under the 24 hour buy-sell agreement. AEP did transmit this power. Seven hours later in the day, St. Mary's Greenup Hydro project power was available and the 8 MW from DP&L was no longer needed. If St. Mary's had been receiving the hourly power that AEP had refused to transmit, St. Mary's could have switched to Greenup power. But because AMP-Ohio had changed to daily service, St. Mary's had to pay a demand charge for the entire day, even though it used the power only 7 hours and would have paid less under the hourly rate. Ex. AMPO-1 at 8-9.

6. In January 1994, AMP-Ohio sought to transfer power from one member with generation to other members, which required transmission over AEP and Toledo Edison lines. Toledo Edison said yes, AEP said no. AMP-Ohio's northern members purchased emergency power from Toledo Edison. AMP-Ohio then reminded AEP that it had agreed not to deny transmission **[31,921]** and AEP agreed to transmit. Ex. AMPO-1 at 9.

7. IMPA arranged to buy 80 MW of short-term power from LG&E and have it wheeled, using buy-sell arrangements, through Public Service Company of Indiana (PSI) and AEP to serve IMPA's load at Richmond (an IMPA

member). The delivered price was $.292 per kW-day plus a 1 mill adder. At the same time AEP arranged to buy 300 MW from PSI at $.30 per kW day plus out-of-pocket energy costs. Hence, PSI was shipping a total of 380 MW to AEP with 80 MW of that amount to be delivered to IMPA's load at Richmond. Then, on a day when IMPA should have received the 80 MW, AEP told IMPA that PSI had sold everything to AEP and that IMPA would have to buy from AEP at $.63 per kW day plus the cost of energy from AEP. IMPA purchased from AEP under protest. AEP used its control over transmission to intercept the 80 MW at a lower price and resell it as short-term power to IMPA. AEP claimed that PSI had terminated its sales to AEP on that day. But the 80 MW was independent of PSI's other sales to AEP and would not have been interrupted if AEP had not interrupted it. IMPA-1 at 7.

8. IMPA has combustion turbines owned by and located at one member, which IMPA would like to connect to the Joint Transmission System owned by IMPA, CINergy and Wabash Valley Power Association. To do so, IMPA needed a metering agreement with AEP, to which AEP would not agree. IMPA-1 at 6.

9. In January 1994, IMPA had power to sell from its turbines when AEP and others needed power. IMPA offered power to AEP but AEP it said could not purchase the power without an existing contract. Moreover, since there was no short-term tariff, IMPA could not sell the power to another utility. IMPA-1 at 6.

10. Another example of the utility engaging in dilatory tactics that raised the customer's transaction costs and

effectively denied transmission is the "sham transaction" provision proposed by AEP. As filed, AEP's tariffs permitted it to deny service merely because a portion of the transmitted power might be used to serve a former retail customer of AEP. See, e.g., Ex. BR&WVP-1 (J. Bertram Solomon testimony, February 23, 1994). (As part of a settlement AEP filed the pro forma tariff and withdrew this provision.)

11. Finally, AEP's originally filed tariff contained a "prodigal customer" provision. Under this provision, transmission customers who sought to convert back to requirements service had to give AEP five years' notice, in which case AEP and the customer would enter into negotiations to determine whether AEP will provide service at all and if so under what rate, terms, and conditions. Ex. S-39 at 1 (Staff testimony). AEP did not require notice from all new customers, only from prodigal customers. Id. at 2. That a potential customer was previously served by AEP is not a reason to treat the customer differently. (AEP withdrew this provision when it filed the pro forma tariff.)

B. *Entergy Services, Inc. (Entergy)*

Entergy filed a partial settlement largely adopting the NOPR pro forma tariffs except for two provisions (headroom and ancillary services). Because the settlement predated the filing date for customer testimony before the ALJ, the customers did not address the need for Entergy to file a tariff. However, customers did make allegations of discriminatory practices, as follows.

1. Customers alleged that Entergy flat-out refused to wheel. Louisiana Energy and Power Authority (LEPA)

witness Sylvan J. Richard testified that LEPA's predecessor systems could not obtain interconnections from Entergy. Ex. SJR-1 at 50.

2. Customers also alleged that Entergy refused to provide service priority equal to native load and refused to provide service flexibility equivalent to the utility's own use. For example, LEPA witness Richard testified that even after state commissions ordered interconnections and other coordination services, LEPA's predecessors were still not able to obtain coordination services because Entergy was not willing to coordinate and because the transmission service it did offer was inflexible, unidirectional point-to-point service, which prevented economic coordination with others. Id. at 50-51.

3. South Mississippi Electric Power Association (SMEPA) witness J. Bertram Solomon testified that Entergy's original "open access" tariff was restricted to **[31,922]** point-to- point service, proposed separate charges for each operating company, and required the cancellation of existing agreements in order to take service under the proposed tariff. Ex. SMEPA-10 at 28. Entergy eventually filed a network tariff, but proposed different local facilities charges for the various Entergy public utility operating subsidiaries. Id. at 29. Since these local facilities charges were higher than the transmission component of the subsidiaries' bundled rates, Entergy obtained a competitive advantage. Id.

4. The Arkansas Cities and Cooperatives (ACC) is a group of cities and cooperatives that own or operate electric generation or distribution systems in Arkansas. ACC Witness Steven Merchant testified that Entergy has segregated the

wholesale market between two of its subsidiaries, Arkansas Power & Light Copmpany (APL) and Entergy Power, Inc. (EPI). Ex. SMM-1 at 16. In marketing power and energy in Arkansas, EPI is subject to an Arkansas Commission order that bars EPI from competing with APL for wholesale loads without first obtaining a waiver. Id. Recently, EPI requested this waiver for all wholesale transactions in Arkansas except for wholesale customers currently served by an Entergy subsidiary; in other words, EPI requested the Arkansas Commission to expand competition for all wholesale customers except where EPI might compete with APL. Id. ACC witness Merchant concluded that, since EPI does not compete with APL, Entergy insulates APL's wholesale business from competition and denies those wholesale customers access to EPI as a source of power, thereby limiting alternative generation sources available to ACC. Id. at 17-19. (Entergy's witness Kenney stated that Entergy has recently filed a joint motion with ACC to the Arkansas Commission seeking to extend the waiver and permit EPI to sell to APL's wholesale customers. Ex. JFK-11 at 14- 15.)

C. *Pacific Gas & Electric Company (PG&E)*

Northern California Power Agency (NCPA) attached several documents to its 1988 complaint in Docket No. EL89-4. These documents were provided to support NCPA's claim that PG&E's unreasonable practices under the PG&E/NCPA Interconnection Agreement (IA) effectively denied NCPA access to transmission properly requested under the IA. Although the parties eventually settled and the Commission terminated the docket with a letter order dated May 18, 1988, these documents provide allegations of PG&E using dilatory

tactics that so protracted negotiations as to effectively equal a refusal to wheel.[3]

1. PG&E stated that since transmission was not currently available, it was entitled to wait 72 months before providing transmission; that is, transmission access could not be granted before the passing of the 72-month notice period. NCPA 1988 Complaint, Ex. 3. However, the IA provided that transmission be provided when it becomes actually available. PG&E also requested substantial additional information, which NCPA considered beyond that reasonably necessary for a study, but still provided. PG&E then determined that transmission was not available, reasoning that transmission was unavailable unless all the transmission requested could be provided 8760 hours per year without restrictions or limitations, extending through the expiration of the agreement in 2013. NCPA 1988 Complaint at 9.

2. On November 27, 1987, NCPA made a new transmission request to PG&E, seeking 50 MW of bi-directional transmission at Midway. NCPA 1988 Complaint, Ex. 5. On January 28, 1988, PG&E filed an interconnection agreement with Turlock Irrigation District (TID) that provided TID with 50 MW of bi-directional transmission at

---

[3]All of these incidents are related to and examples of PG&E's conduct described in the NOPR (*FERC Statutes and Regulations* ¶32,514 at p. 33,073 n.151), that is, the history of PG&E's attempt to avoid its commitments made to the California owners of the California Oregon Transmission Project (COTP). However, these incidents are not exactly the same as the incidents described in the NOPR, because NCPA is not one of the owners of the COTP.

Midway. Pacific Gas & Electric Company, 42 FERC para. 61,406, order on reh'g, 43 FERC para. 61,403 (1988). On February 22, 1988, PG&E advised NCPA that all firm transmission service available at Midway had **[31,923]** been fully subscribed. NCPA 1988 Complaint, Ex. 6. Then, on March 29, 1988, PG&E filed with the Commission an interconnection agreement with Modesto Irrigation District (MID), that provided MID with 50 MW of bi-directional transmission at Midway. Pacific Gas & Electric Company, 44 FERC para. 61,010 (1988). At about the same time (in the last week in March 1988), PG&E advised NCPA that the allocations of transmission to TID, MID, and others, including a not yet finalized allocation to Sacramento Municipality Utility District, had used all the transmission available at Midway. NCPA 1988 Complaint, Exs. 7 and 8.

D. *Northeast Utilities Service Company (NU)*

This is the case where Northeast Utilities acquired Public Service of New Hampshire (PSNH) (Docket No. EC90-10). New England Power Company (NEP) witness Robert Bigelow's direct testimony expressed concern over the "relatively restrictive transmission policies of both" NU, on behalf of Northeast Utilities' public utility subsidiaries, and PSNH. Bigelow Direct Testimony at 21 (filed May 25, 1990). In his cross rebuttal testimony, Mr. Bigelow testified that "NU has a poor track record as a provider of transmission service" and "PSNH also has an abhorrent track record as a provider of transmission services." Bigelow Cross Rebuttal Testimony, at 3 (filed June 20, 1990). Mr. Bigelow described both NU's and NEP's (his own company) failure to provide service flexibility equivalent to their own use. Except for NEP's TDUs, both NEP and NU historically provided only

point-to-point transmission, which required separate scheduling for each transaction. Bigelow Cross Rebuttal at 4.

E. *Southern California Edison Company and San Diego Gas and Electric Company*

The evidence in this merger proceeding (Docket No. EC89-5) included testimony from a number of witnesses describing instances of Edison's conduct. Richard Greenwalt was the power supply supervisor for the City of Riverside, California. He was responsible for scheduling all purchases of energy for Riverside and for the cities of Azusa, Banning and Colton, California. Greenwalt testimony at 1 (November 1989). (These four cities and Anaheim, California, are collectively referred to as the Southern Cities or Cities.) Joseph Hsu was the Director of Utilities for Azusa. Hsu testimony at 1 (November 1989). Gale Drews was the electric utility director of Colton. Drews testimony at 1-2 (November 1989). Bill Carnahan was the director for Riverside. Carnahan testimony at 1 (November 1989). Gordon Hoyt was the general manager of the Anaheim power department. Hoyt testimony at 1 (November 1989). Dan McCann was the power coordination supervisor for Anaheim. He supervised Anaheim's load scheduling and is a former Edison employee, having worked for Edison for 20 years. McCann Testimony at 1-2 (November 1989). These witnesses testified that Edison refused to wheel as follows.

1. Edison's policy was to curtail the Cities any time it could be justified using any of a list of acceptable reasons to deny interruptible transmission service. Id. at 22-23.

2. Edison would not generally provide transmission service when Edison could save money by itself purchasing the economy energy that would be wheeled. McCann testimony at 19. The Cities called Edison every hour to request interruptible transmission service. Id.. Edison often refused to sell energy available in the Western Systems Power Pool to the Cities and then made available higher cost contract energy or partial requirements service. Id. at 19-20.

3. When Anaheim requested Edison provide firm transmission of power from neighboring states, Edison would often agree to provide non-firm service but would not integrate the capacity for many years in the future, saying that its control area did not need capacity at that time. Hoyt testimony at 9. Since the selling utility was interested in a sale of capacity, not just energy, the transaction would not occur. Id. Edison repeatedly used its control over transmission to deny Anaheim access to low-cost firm power. Id. at 9-10.

4. While Edison provided short-term firm transmission service to the Cities, it would only provide long-term firm service for three specific resources: The SONGS nuclear plant, a specific IPP, and Hoover Dam power. Hoyt testimony at 20. One of Edison's reasons for denying long-term transmission was that Edison desired to **[31,924]** reserve the transmission for its own future (unspecified) needs. Id.

5. In the 1970s, Edison refused to allow the Cities access to the Pacific Intertie. Hoyt testimony at 21; Drews testimony at 7-8.

6. In 1988, Edison refused to provide transmission service for a Cities power purchase from Public Service

Company of New Mexico (PSNM) from Palo Verde Nuclear station. Hoyt testimony at 21.

7. Edison has refused to provide requested firm transmission from

--California-Oregon border to Midway Station

--Nevada-Oregon Border to Sylmar Substation

--Palo Verde Switchyard to Vista

--SONGS Switchyard to Vista.

Carnahan testimony at 15.

8. Riverside requested transmission from Palo Verde and was told that such service was not available. Carnahan testimony at 16. Edison offered Riverside only 12 MW of curtailable transmission entitlement to provide Riverside's share of Palo Verde. Id. This service was neither large enough or long enough, and Edison insisted on unreasonable terms and conditions. Id.

9. Azusa, Banning and Colton had a contract with Edison that entitled them to use their Palo Verde firm transmission path to schedule energy to meet their contract energy obligation. Edison refused to permit the three cities to use that path. Edison did not contest that the contracts allowed this use, but said that the scheduling of such small amounts of energy for the three cities would be too burdensome. Greenwalt testimony at 14.

10. Edison would not respond in a timely manner to the Cities' requests, routinely taking months to respond. Drews testimony at 15.

11. During the 1980s, Edison provided Colton with some transmission service to allow the Cities to reach certain suppliers, but limited the choices available to the Cities and imposed terms and conditions that increased the Cities' costs and placed Colton at a disadvantage against Edison. Drews testimony at 9. Arranging alternative generation sources was difficult because the Cities always had to first get Edison to state whether it would provide transmission.

12. During 1988 and 1989, a dispute arose between Edison and the Cities concerning the Hoover Uprating Project. Drews testimony at 16. Edison argued that for the months when units were out of service for uprating, and Southern Cities capacity was reduced to zero, Southern Cities would not receive an energy credit, even though energy was still available and used by Edison. But the contracts allowed a participant who did not have capacity to still schedule its energy as non-firm energy on the capacity of another participant. Id. at 16-17.

13. In 1986, Azusa negotiated a power purchase contract with the California Department of Water Resources in increments of first 5 MW and then 2 MW (for a total of 7 MW). Hsu testimony at 14. First Edison assured Azusa that the transmission for the additional 2 MW would not be a problem. Id. Then Edison would not agree to amend the transmission service agreement for the additional 2 MW. Id.

14. In 1986, Azusa notified Edison of Special Condition 12[4] purchases from PG&E and requested firm transmission service. Id. Two months before service was to begin, Edison notified the Cities of a problem with the transmission lines. Id. Transmission was eventually granted, but only after a four-month delay and substantial losses to the Cities. Id. Then Edison decided there was no problem with its transmission facilities. Id. at 14-15.

15. In 1986-87, the Cities purchased 20 MW from PG&E and 80 MW from Deseret G&T Cooperative. Hoyt testimony at 7-8. Edison stated that without reinforcement of its transmission system, Edison would not provide the transmission. Id. There was a five-month delay during which the Cities were forced to purchase from Edison at a higher cost. Id. at 8-9. Then Edison decided that the transmission system did not need reinforcement. Id. at 8.

[31,925]

16. Edison also refused to provide a service priority equal to that of native load. It would curtail the Cities in order to purchase more economy energy for itself. McCann testimony at 28. If Edison could make the purchase, it would curtail the City and use the energy for itself. Id. When Edison curtailed the Cities, they were not able to purchase economy energy and instead purchased energy from Edison. Id. at 24.

---

[4]Special Condition 12 of the Integrated Operations Agreement between Edison and the Southern Cities defined certain Special Condition 12 resources and allowed the Cities to make certain uses of those resources, subject to certain restrictions.

17. According to Edison, the interruptible transmission it provided the Cities was interruptible for any reason. Id. at 20. A purchase could be terminated the hour after it is begun or even during the hour. Id. As a result, the Cities lost opportunities to make advantageous economy purchases. Id. at 20-21.

18. Edison also refused to provide customers flexibility similar to the flexibility Edison provided itself. Edison's refusal to provide bi-directional transmission service restricted the Cities' abilities to purchase hydroelectric energy from the Pacific Northwest. Hoyt testimony at 22. Because most contracts with Northwest utilities require a return of power, the Northwest utilities would not deal with the Cities without transmission to return energy. Id. at 22-23. Edison did provide bi- directional transmission to the Los Angeles Department of Water & Power (LADWP) to accommodate flows to and from Arizona. Id.

19. Riverside was unable to obtain non-firm service more than two hours in advance of need. Carnahan testimony at 18.

20. Riverside and Colton were both served out of Edison's Vista substation. Although the two cities were on the same 69 kV bus, Edison would not allow them to sell energy to each other. Greenwalt testimony at 17.

21. Riverside's agreement with Edison allowed Riverside to purchase a block of energy through the WSPP and divide it up among the four Cities (Azusa, Banning, Colton and Riverside). Greenwalt testimony at 17. When Riverside had excess energy from other sources, Edison

would not permit it to sell that energy to the other three cities. Id. For example, Riverside attempted to sell Deseret energy transmitted by LADWP to the Edison system. Id. at 17-18. LADWP would not break out the Cities' shares of that energy, and Edison would not accept the energy as a delivery for all four cities. Id. at 18. Edison argued that because this energy was excess energy that Riverside could not use, Riverside did not have transmission rights to bring it into the control area. Id. As a result, Riverside paid for the energy delivered by LADWP to the Edison control area, but could not sell it to the other three cities, and gave it to Edison itself, which consumed the energy without making any payment for it. Id. Riverside tried a number of alternative paths, including using WSPP transmission where Riverside paid Edison 5 mills to connect to Azusa, 5 mills to connect to Banning, and 5 mills to connect to Colton for each megawatthour. While this approach was successful for a while, eventually Edison refused to permit these sales.

22. Edison claimed that the Cities only have transmission rights to bring in enough Special Condition 12 energy to satisfy the Cities' load. Greenwalt testimony at 18.

23. Edison contended that the Cities' load requirements were satisfied first by integrated resources and then by Special Condition 12 and economy energy purchases. Id. at 19. When the Cities' integrated resources exceeded their load, any Special Condition 12 resources became excess. Under Riverside's Deseret contract, the Cities were required to take a minimum of 35 MW each hour. Id. Edison acknowledged that it was obligated to buy, or allow the Cities to sell, any excess energy from Riverside's integrated resources. Id. However, Edison refused to give the Cities

credit for excess Special Condition 12 energy brought into the area, claiming that the Cities could not have brought it in because they did not have transmission rights. Id.

II. Other Examples of Transmission Disputes

Disputes over transmission are not uncommon, contrary to EEI's suggestion. Some recent examples taken from pleadings and other documents and from Commission orders reveal that it has been very difficult for various entities in the electric power industry to agree on transmission rights. These examples also reveal that even after issuance of AEP and the Open Access NOPR with its proposed pro forma tariffs, there has been considerable controversy over whether various utilities' **[31,926]** "open access" tariffs deviate from those tariffs. (The Commission has allowed utilities that adopt tariffs that match or exceed the non-rate terms and conditions in the NOPR pro forma tariffs to obtain certain benefits.)

A. In a letter of February 3, 1995 to Mr. Gerald Richman of the Commission's Enforcement section in the Office of the General Counsel, Steven J. Kean, Vice President, Regulatory Affairs, Enron Power Marketing, Inc. (Enron) alleged that Niagara Mohawk Power Corporation (NiMo) refused to wheel power from Rochester Gas & Electric (RG&E) to Enron under RG&E's transmission contract with NiMo; however, when Enron revealed the buyer, NiMo did wheel power for RG&E to the buyer. Mr. Kean alleged that this was not an isolated incident. NiMo argued that the contract did not require it to provide RG&E with transmission to Enron. It also said that the principle of comparability does not require the service. Letter of

November 21, 1994 from NiMo representative A. Karen Hill to Gerald Richman.

B. The Commission's Task Force Hot Line (Hot Line) received a complaint that a member of the New York Power Pool (NYPP) refused to transmit power that another member bought from a power marketer. In a letter of November 17, 1994, from Chair Moler to Mr. William J. Balet, Executive Director of NYPP, Chair Moler explained that the Commission's enforcement staff had investigated and found the allegation to be true.

C. In Southern Minnesota Municipal Power Agency v. Northern States Power Company (Minnesota), 73 FERC 61,350 (1995), NSP and SMMPA had a contract under which NSP agreed to provide transmission service. However, the parties had numerous disputes over the service. The Commission found that NSP had misinterpreted the contract in several ways. For, example, SMMPA argued that it should be able to directly schedule its deliveries of energy out of the NSP control area and that it should not be limited to particular points of delivery. NSP argued that only it was entitled to control the physical operation of scheduling. The Commission found that the clear language of the contracts gave SMMPA the authority to schedule its own power.

D. Mid-Continent Area Power Pool, 72 FERC para. 61,223 (1995), involved MAPP's membership criteria, which made it impossible for a power marketer to join MAPP and obtain the benefits of certain transmission services available only to MAPP members. The Commission found that the membership criteria may be unreasonable, particularly since

there may be less burdensome ways of setting up membership criteria for non-traditional entities.

* * * * *

[pp. 31,966 - 31,981]

[31,966]

APPENDIX G

I. Legal Analysis of Commission Jurisdiction Over the Rates, Terms and Conditions of Unbundled Retail Transmission in Interstate Commerce

Based on an analysis of the relevant legislative history and case law under the Federal Power Act (FPA), the Commission concludes that it has exclusive jurisdiction over the rates, terms and conditions of the unbundled transmission in interstate commerce, by a public utility, of electric energy to an end user. This is also known as retail wheeling in interstate commerce.[1]

The Commission's jurisdiction over the rates, terms and conditions of transmission in interstate commerce derives

---

[1]Section 212(h) of the FPA provides that no order issued under the FPA shall be conditioned upon or require the transmission of electric energy directly to an ultimate consumer. 16 U.S.C. §824k(h). The Commission's assertion of jurisdiction in this final rule is over the rates, terms and conditions of retail transmission that occurs voluntarily or as a result of a state retail access program.

from Congress' power to regulate interstate commerce under the United States Constitution[2] and the FPA. When Congress enacted the FPA, it gave the Commission exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. The Supremacy Clause of the Constitution provides that federal laws enacted pursuant to the powers delegated to the federal government by the United States Constitution are the supreme law of the land.[3] Accordingly, to the extent that retail wheeling involves transmission in interstate commerce by public utilities, the rates, terms and conditions of such service are subject to the exclusive jurisdiction of the Commission, and must be filed with the Commission.[4]

1. Relevant Federal Power Act Provisions

Section 201(b)(1) of the FPA provides:

> The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce * * *. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction * * * over facilities used in local distribution or only for the transmission of electric energy in

---

[2]U.S. Const. art I, Section 8, cl.3.

[3]U.S. Const. art. VI, cl.2.

[4]*See Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246, 251-52 (1951) (*Montana-Dakota*).

intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

16 U.S.C. 824(b)(1) (emphasis added). Thus, the statute on its face limits Commission jurisdiction over sales of energy to sales at wholesale, but does not limit jurisdiction **[31,967]** over transmission to transmission used only for wholesale sales.

Sections 201(c) and (d) define the meaning of "the transmission of electric energy in interstate commerce" and "sale of electric energy at wholesale in interstate commerce." Section 201(c) provides:

For the purpose of this Part, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof: but only insofar as such transmission takes place within the United States.

16 U.S.C. 824(c). Section 201(d) provides:

The term "sale of electric energy at wholesale" when used in this Part means a sale of electric energy to any person for resale.

16 U.S.C. 824(d).

Sections 205 and 206 of the FPA give the Commission jurisdiction over the rates, terms and conditions of transmission in interstate commerce, and sales at wholesale in interstate commerce, by public utilities. 16 U.S.C. 824d and 824e.

2. Legislative History and Case Law

Much of the legislative history of the FPA indicates that Congress intended the Commission's jurisdiction to extend only to those matters which the Attleboro decision[5] held to be beyond the reach of the States. For instance, the report accompanying the Senate bill states that subsection (b) "leaves to the States the authority to fix local rates even in cases where the energy is brought in from another State."[6] In other words, states retain authority to regulate rates of electric energy to ultimate consumers. The Senate report also states:

The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in (Attleboro) to be beyond the reach of the States. Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines and over the generating facilities which produce energy[7] for interstate transmission and sale.

---

[5]*Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927) (Attleboro). In Attleboro, the Supreme Court held that State regulation of the interstate sale of electricity was barred by the Commerce Clause because such regulation would impose a "direct burden" on interstate commerce.

[6]S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). See also H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935).

[7]The provisions of the Senate bill regarding federal jurisdiction over generating facilities were eliminated from the final version of the bill.

S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935) (emphasis added). Thus, federal jurisdiction over transmission lines is not dependent on whether those lines are used to effect a sale, wholesale or otherwise.

The provisions of FPA section 201 reserving certain regulatory authority to the States have been interpreted narrowly.[8] The Supreme Court has stated:

In section 201(b), Congress did no more than leave standing whatever valid state laws then existed relating to the exportation of hydroelectric energy; by its plain terms, 201(b) simply saves from pre-emption under Part II of the Federal Power Act such state authority as was otherwise "lawful."[9]

---

[8]Section 201(a) declares that Federal regulation of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, "such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States." 16 U.S.C. §824(a). Section 201(b)(1) states that the provisions of Part II of the FPA apply to the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce but, except as specifically provided, "shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line." 16 U.S.C. §824(b)(1).

[9]*New England Power Co. v. New Hampshire*, 455 U.S. 331, 341 (1982) (NEPCO).

The Court also stated:

Nothing in the legislative history or language of the statute evinces a congressional intent 'to alter the limits of state power otherwise imposed by the Commerce Clause,' * * * or to modify the earlier holding of this Court concerning the limits of state authority to restrain interstate trade.[10]

[31,968]

Unlike the narrow interpretations given to the FPA provisions reserving certain regulatory authority to the States,[11] the courts have construed transmission "in interstate commerce" broadly. The term does not turn on whether the contract path for a particular power or transmission sale crosses state lines, but rather follows the physical flow of electricity. Because of the highly integrated nature of the electric system, this results in most transmission of electric energy being "in interstate commerce."

One of the earliest cases construing Commission jurisdiction over transmission was Jersey Central Power & Light Co. v. FPC, 319 U.S. 61 (1943) (Jersey Central). In that case, the Commission asserted jurisdiction over a New

---

[10]*Id.* (citation omitted).

[11]While Congress may exercise its Commerce Clause authority to grant the States that "ability to restrict the flow of interstate commerce that they would not otherwise enjoy," Lewis v. BT Investment Managers, Inc., 447 U.S. 27, 44 (1980), States may not exercise such regulatory powers unless Congress has expressly stated its intention to make such an affirmative grant of power. *NEPCO*, 455 U.S. at p. 343.

Jersey utility by showing that the utility owned transmission facilities that were used to transmit energy in interstate commerce. The Court found that the Commission had demonstrated that the utility owned transmission facilities that were indirectly interconnected, through a second New Jersey utility, to facilities owned by a New York utility and that the facilities were used to transmit electric energy in interstate commerce.

The Court noted that section 201(c) of the FPA defines electric energy transmitted in interstate commerce to be energy "transmitted from a State and consumed at any point outside thereof." The Court stated:

It is impossible for us to conclude that this definition [of transmission in interstate commerce] means less than it says and applies only to the energy at the instant it crosses the state line and so only to the facilities which cross the line and only to the company which owns the facilities that cross the line.

319 U.S. at 71. Thus, a critical question regarding the jurisdictional status of a wheeling transaction is whether the facilities used to provide the service transmit electric energy in interstate commerce.

In Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) (CL&P), the Court reviewed the Commission's finding that a Connecticut utility was jurisdictional because it owned transmission facilities that were used in interstate commerce. The Court generally embraced the Jersey Central standard for determining whether facilities are used to transmit electric energy in interstate commerce. The Court

emphasized that whether certain facilities transmit electric energy in interstate commerce is more a technical than a legal question. The Court stated:

Federal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test.

324 U.S. at 529. Thus, the Court adopted the Jersey Central test providing that the Commission's jurisdiction generally extends to transmission facilities that transmit electric energy in interstate commerce.

The Court also applied the Jersey Central test in FPC v. Florida Power & Light Co., 404 U.S. 453 (1972), affirming the Commission's finding of jurisdiction over a Florida utility. The Commission demonstrated that the utility transmitted power to another Florida utility's "bus"[12] that power was simultaneously transferred from the "bus" to a Georgia utility. The Court upheld the Commission's finding that electric energy from the two Florida utilities was commingled and was therefore transmitted in interstate commerce. 404 U.S. at 463.

In all of the above cases, the Court's decisions turned on whether energy being transmitted flowed in interstate commerce as a technical matter. The decisions did not turn on

---

[12]A bus is an electrical conductor which serves as a common connection for two or more electrical circuits. Electric Utility Rate Design Study, Glossary: Electric Utility and Ratemaking Load & Management Terms, Edison Electric Institute (Sept. 11, 1978).

whether the transmission of energy flowing in interstate commerce involved energy that was being sold for resale or was being sold to **[31,969]** an end user. Thus, there is nothing in the statute, its legislative history, or the case law to indicate that the Commission's jurisdiction over rates, terms and conditions of transmission in interstate commerce extends only to wholesale transmission and not retail transmission. Indeed, the statute on its face gives the Commission jurisdiction over transmission in interstate commerce and makes no distinction between wholesale transmission and retail transmission.

However, there are two important limitations on Commission authority. First, as discussed above, the FPA does not give the Commission jurisdiction over sales of electric energy at retail. Such sales historically have been bundled sales (i.e., generation and transmission), and courts and the Commission have recognized State jurisdiction over bundled sales of energy. Second, under section 201(b)(1) of the FPA, the Commission does not have jurisdiction over facilities used in local distribution. In CL&P, the Court stated that local distribution facilities are exempt from Commission jurisdiction even if those facilities "carry no energy except extra-state energy." 324 U.S. at 531.

In the next section the Commission further discusses the statutory provisions and case law that shed light on the demarcation between transmission and local distribution, and thus on the jurisdictional line between federal and State authority.

II. Legal Analysis of Commission Jurisdictional Transmission Facilities and State Jurisdictional Local Distribution Facilities

Two specific circumstances are addressed:

First, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to a purchaser who will then re-sell the energy to an end user?

Second, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to an end user?

Based on an analysis of the relevant legislative history and case law under the FPA, the Commission reaches the following conclusions. With respect to the first circumstance, the Commission concludes that a public utility's facilities used to deliver electric energy to a wholesale purchaser, whether labeled "transmission," "distribution," or "local distribution" are subject to the Commission's exclusive jurisdiction under sections 205 and 206 of the FPA, and that a public utility's facilities used to deliver electric energy from the wholesale purchaser to the ultimate consumer are "local distribution" facilities subject to the rate jurisdiction of the state.[13]

---

[13]There are, of course, facilities that are used to provide delivery to both wholesale purchasers and end users. In those situations, we believe that the Commission and the States have

With respect to the second circumstance, the Commission believes that, based on the particular facts of the case, some of the public utility's facilities used to deliver electric energy to an end-user may be FERC-jurisdictional transmission facilities, while some of the facilities used may be state-jurisdictional local distribution facilities.

We set forth below the relevant legislative history and case law, our legal conclusions, and the factors which we believe are indicative of whether facilities are used in "local distribution" or "transmission in interstate commerce," as those terms are used in the FPA.

1. Relevant Federal Power Act Provisions

The Commission's jurisdiction is set forth in section 201 of the FPA.[14] Section 201(b)(1) provides in pertinent part:

> The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce * * *. The Commission shall have jurisdiction over all facilities for **[31,970]** such transmission or sale of electric energy, but shall not have jurisdiction * * * over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for

---

jurisdiction to set rates for the services that are within their respective jurisdictions. That facilities are used to serve resale and retail customers does not, however, necessarily mean that the facilities are local distribution facilities.

[14]16 U.S.C. §824.

> the transmission of electric energy consumed wholly by the transmitter.[15]

Some of the court decisions that construe jurisdictional facilities under section 201 also construe the Commission's jurisdiction under section 203. Section 203(a) provides, in relevant part:

> No public utility shall sell, lease, or otherwise dispose of the whole of its facilities subject to the jurisdiction of the Commission, * * * or by any means whatsoever, directly or indirectly, merge or consolidate such facilities or any part thereof with those of any other person * * * without first having secured an order of the Commission to do so.[16]

In addition, section 206(d) concerns facilities "under the jurisdiction of the Commission":

> The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.[17]

---

[15]16 U.S.C. §824(b) (emphasis added).

[16]16 U.S.C. §824b (emphasis added).

[17]16 U.S.C. §824e(d) (emphasis added).

2. Legislative History of the FPA

The relevant legislative history of the general purposes of Title II of the FPA, and of section 201 in particular, focuses primarily on bundled sales of electric energy and does not directly address the issue of what constitutes local distribution as opposed to transmission in interstate commerce.

In discussing the general purposes of Title II of the House bill, the House Report states:

Title II * * * establishes for the first time regulation of electric utility companies transmitting energy in interstate commerce.

* * * * *

* * * Under the decision of the Supreme Court of the United States in (Attleboro), the rates charged in interstate wholesale transactions may not be regulated by the States. Part II gives the Federal Power Commission jurisdiction to regulate these rates. A "wholesale" transaction is defined to mean the sale of electric energy for resale and the Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce.[18]

[18]H.R. Rep. No. 1318, 74th Cong., 1st Sess. 7-8 (1935).

In its analysis of section 201, the House Report states:

As in the Senate bill no jurisdiction is given over local distribution of electric energy, and the authority of States to fix local rates is not disturbed even in those cases where the energy is brought in from another State.[19]

The Senate Report's discussion of the general purposes of the FPA states:

The decision of the Supreme Court in [Attleboro] placed the interstate wholesale transactions of the electric utilities entirely beyond the reach of the States. Other features of this interstate utility business are equally immune from State control either legally or practically.[20]

In discussing material differences between the final version of the Senate bill and the original version, the Senate Report states:

Subsection (b), formerly (a), which states the subject matter to which the part relates, has been clarified to make plain that it includes interstate transmission where there is no sale and excludes **[31,971]** all facilities used only for

[19]*Id.* at p. 27.

[20]S. Rep. No. 621, 74th Cong., 1st Sess. at p. 17 (1935). See id. at p. 18 ("The revision [between the original and final versions of the Senate bill] has also removed every encroachment upon the authority of the States. The revised bill would impose Federal regulation only over those matters which cannot effectively be controlled by the States.")

production of transmission in intrastate commerce or in local distribution.[21]

In discussing section 201 of the Senate bill, the Senate Report further states:

The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in (Attleboro) to be beyond the reach of the States. Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines and over the generating facilities which produce energy for interstate transmission and sale. It is obvious that no steps can be taken to secure the planned coordination of this industry on a regional scale unless all of the facilities, other than those used solely for retail distribution, are made subject to the jurisdiction of the Commission. Facilities used only for intrastate commerce or local distribution are expressly excluded from the operation of the act.[22]

The Conference Report adds little description regarding jurisdictional facilities. In reference to section 201(b) it states that:

[T]he language of the House amendment has been followed with a clarifying phrase added to remove any doubt as to the Commission's jurisdiction over facilities used for the

---

[21] *Id.* at p. 19.

[22] *Id.* at p. 48. The provisions of the Senate bill regarding federal jurisdiction over generating facilities were eliminated from the final version of the bill.

generation and local distribution of electric energy to the extent provided in other sections of this part and the part next following.[23]

In addition to the above statements pertaining to section 201 of the FPA, Congress referenced distribution of energy in the legislative history of section 206(d). Section 206(d) was originally enacted as section 206(b) of the FPA. Under the Regulatory Fairness Act of 1988,[24] section 206(b) was redesignated as section 206(d).

The Conference Report on the original FPA does not address section 206(b). The Senate Report on the FPA bill states in pertinent part:

Subsection (b) authorizes the Commission to investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy. * * * Since the rate-making powers granted to the Commission apply only to the wholesale rates of energy sold in interstate commerce, this last subsection should be of great benefit in removing the practical difficulty which the States may encounter in regulating the interstate distribution rates which are left under their control. Such rate regulation involves the examination and valuation of property outside the State. The task is one requiring an agency with a

---

[23] H.R. Conf. Rep. No. 1903, 74th Cong., 1st Sess. 74 (1935).

[24] Pub. L. No. 100-473, 102 Stat. 2299 (1988).

jurisdiction broader than that of a single State. The authority of the Federal Commission is to render assistance to the State commissions in a way which would preserve and make more effective the jurisdiction which is thus left to the States.[25]

The House Report discusses section 206(b) as follows:

This subsection reaches those situations where electric energy is transmitted in interstate commerce by the same company which distributes it locally, and will greatly aid State commissions in fixing reasonable rates in such cases.[26]

Thus, the discussions in the two reports do not appear to contemplate a situation in which the transmitter and seller of electric energy are different, and neither is a "local" distributor. The House Report expressly refers to the same company being the transmitter and seller of electric energy. The Senate Report by its terms addresses the regulation of interstate distribution rates.[27]

---

[25]S. Rep. No. 621, 74th Cong., 1st Sess. 51 (1935) (emphasis added).

[26]H.R. Rep. No. 1318, 74th Cong., 1st Sess. 29 (1935) (emphasis added).

[27]The Senate Report states that interstate distribution rates are left in the States' control. Obviously, the Senate drew a distinction between interstate distribution (left in the States' control) and interstate transmission (given to the FPC). Compare S. Rep. No. 621 at p. 49 with H.R. Rep. No. 1318 at p. 51.

The above legislative history on sections 201 and 206(b) does not provide any **[31,972]** definitive answers to the questions raised. We therefore turn to the case law under the FPA.

3. Case Law Under the FPA

Jersey Central was the first of the major FPC jurisdictional cases considered by the Supreme Court. The case involved the acquisition by New Jersey Power and Light Company (New Jersey Power) of certain securities of Jersey Central Power & Light Company (Jersey Central) without the Commission's prior approval. The question before the Court was whether Jersey Central was a "public utility" under section 201(e)[28] of the FPA so that the Commission's prior approval of the stock acquisition was necessary under section 203 of the FPA.

Jersey Central owned transmission facilities that connected to facilities that Public Service Electric & Gas Company (Public Service) owned. The interconnection of these transmission facilities was in New Jersey. Public Service's facilities in turn connected to the facilities of the Staten Island Edison Corporation (Staten Island Edison), a New York utility, at the mid-channel of Kill van Kull, a body

---

[28]Section 201(e) defines a "public utility" as "any person who owns or operates facilities subject to the jurisdiction under this Part (other than facilities subject to such jurisdiction solely by reason of section 210, 211, or 212)." 16 U.S.C. §824(e). The section as adopted in 1935 did not contain the parenthetical, which was adopted in 1978 as part of the Public Utility Regulatory Policies Act.

of water separating New Jersey and New York. Jersey Central delivered energy to and received energy from Public Service under contract, and Public Service delivered energy to and received energy from Staten Island Edison under contract.[29]

The Court found that, although Jersey Central generated and received electricity only in New Jersey, some of the electric energy that it dispatched to Public Service "was instantaneously transmitted to New York."[30] The Court held that "[t]his evidence * * * furnishes substantial basis for the conclusion of the Commission that facilities of Jersey Central are utilized for the transmission of electric energy across state lines."[31] Therefore, the Court found that Jersey Central was a public utility within the meaning of section 201(e).[32]

The Court cited Attleboro, in which the Court found that the sale of locally produced electric energy for use in another state resulted in the transmission of electric energy in interstate commerce, even though title passed at the state line.[33] In Jersey Central, the Court explained the rationale for federal jurisdiction as follows:

---

[29]Jersey Central, 319 U.S. at pp. 63-65.

[30]*Id.* at p. 66.

[31]*Id.* at p. 67 (citation omitted).

[32]*Id.* at p. 73.

[33]273 U.S. at pp. 86, 89-90.

(Section 201(c) of the FPA) defines the electric energy in commerce as that "transmitted from a State and consumed at any point outside thereof." There was no change in this definition in the various drafts of the bill. The definition was used to "lend precision to the scope of the bill." It is impossible for us to conclude that this definition means less than it says * * *. The purpose of this act was primarily to regulate the rates and charges of the interstate energy.[34]

The Court in Jersey Central thus interpreted the FPA as placing within the federal province regulation of wholesale sales of electric energy that, in any manner, flows in interstate commerce. The language quoted above and the citation to section 201(c) of the FPA, to be relied upon in subsequent Supreme Court cases, strongly suggested that the Commission's jurisdiction was not based on whether there was a sale by the utility, but rather on the flow of electric energy either into or out of a state, so long as the energy crosses state lines.

CL&P, which was decided two years after Jersey Central, is the leading case interpreting the section 201(b) local distribution proviso. In CL&P, the Commission sought to regulate the accounting practices of Connecticut Light & Power Company (CL&P).[35] At issue was whether **[31,973]** CL&P was a "public utility" under the FPA. The utility's system encompassed an area solely within a single state

---

[34]319 U.S. at p. 71 (footnote omitted).

[35]CL&P, 324 U.S. at p. 517.

(Connecticut)[36] and did not interconnect with any other company that operated out of state.[37] "Its purchases and sales, its receipts and deliveries of power, [were] all within the state."[38] However, CL&P did purchase energy from companies that had, in turn, purchased energy from Massachusetts. The company also sold energy to a municipality that exported a portion of that energy to Fishers Island, located off the coast of Connecticut but "territory of New York."[39] The Commission based its jurisdiction on these few transactions.[40]

The Court of Appeals affirmed the Commission, holding that the Commission's jurisdiction extended to "electric distribution systems which normally would operate as interstate businesses." The Court of Appeals found that:

> Whether or not the facilities by which petitioner distributes energy from Massachusetts should be classified as 'local' is not relevant to this case. The sole test of jurisdiction of the Commission over accounts is whether these facilities,

---

[36]*Id.* at p. 518.

[37]*Id.* at p. 521.

[38]*Id.* at p. 522.

[39]*Id.* at pp. 519-21.

[40]*Id.*

> 'local' or otherwise, are used for the transmission of electric energy from a point in one state to a point in another.([41])

The Supreme Court reversed. It held that the statutory language in section 201(b) of the FPA providing that the Commission "shall not have jurisdiction * * * over facilities used in local distribution" is a limitation upon Commission jurisdiction that "the Commission must observe and the courts must enforce."[42] In analyzing the statute, the Court stated:

> It has never been questioned that technologically generation, transmission, distribution and consumption are so fused and interdependent that the whole enterprise is within the reach of the commerce power of Congress, either on the basis that it is, or that it affects, interstate commerce, if at any point it crosses a state line.
>
> * * * * *
>
> But whatever reason or combination of reasons led Congress to put the provision in the Act, we think it meant what it said by the words "but shall not have jurisdiction * * * over facilities used in local distribution." Congress by these terms plainly was trying to reconcile the claims of federal and local authorities and to apportion federal and state jurisdiction over the industry.[43]

---

[41]*Id.* at p. 522, *quoting Connecticut Light & Power Co. v. FPC*, 141 F.2d 14, 18 (D.C. Cir. 1944).

[42]324 U.S. at p. 529.

[43]*Id.* at pp. 529-31.

The Court decided that this limitation on jurisdiction was "a legal standard that must be given effect in this case in addition to the technological transmission test."[44]

The Court stated that whether or not local distribution facilities carried out-of-state electric energy was irrelevant. Whatever the origin of the electric energy they carried, so long as the utility used the lines for local distribution,[45] they were exempt from federal jurisdiction.[46] In fact, the Court stated that local distribution facilities "may carry no energy except extra-state energy and still be exempt under the Act." Id. at 531. The Court concluded that the Commission's order:

> Must stand or fall on whether this company owned facilities that were used in transmission of interstate power and which were not facilities used in local distribution.[47]

Upon reversing the Court of Appeals, the Court commented, in dictum, on the evidence the Commission had relied upon in finding that the facilities in question were used for transmission. It noted that the Commission had relied upon certain gas transportation cases in concluding that transmission extends from the generator to the point where the

---

[44]*Id.* at p. 531.

[45]It appears that while the Company received power (at one location) at 66 kV, it primarily owned facilities at 13.8 kV and below.

[46]324 U.S. at p. 531.

[47]*Id.* at p. 531 (emphasis added).

function of conveyance in bulk over distance is completed **[31,974]** and the process of subdividing the energy to serve ultimate consumers, which is the characteristic of "local distribution," is begun. The Court cautioned:

> But a holding that distributing gas at low pressure to consumers is a local business is not a holding that the process of reducing it from high to low pressure is not also part of such local business. In so far as the Commission found in these cases a rule of law which excluded from the business of local distribution the process of reducing energy from high to low voltage in subdividing it to serve ultimate consumers, the Commission has misread the decisions of this Court. No such rule of law has been laid down.[48]

The Court also noted in its dictum, however, that once a company is properly found to be a "public utility" under the Act, the fact that a local commission may also have jurisdiction does not preclude exercise of the Commission's functions. Id. at 533.[49] The Court instructed the lower court

---

[48]*Id.* at p. 534.

[49]*See United States v. Public Utilities Commission of California*, 345 U.S. 295, 316 (1953) (Public Utilities Commission): Certainly the concrete fact of resale of some portion of the electricity transmitted from a state to a point outside thereof invokes federal jurisdiction at the outset, despite the fact that the power thus used traveled along its interstate route "commingled" with other power sold by the same seller and eventually directly consumed by the same purchaser-distributor.

See also Arkansas Power & Light Co. v. FPC, 368 F.2d

to remand the case to the Commission for a finding regarding whether the facilities in question were used in local distribution.[50]

The CL&P case was ultimately disposed of without the Commission having made a finding that the facilities were used in local distribution. While the Commission found that it was "extremely doubtful" that it could find that the facilities in question were not local distribution facilities, 6 FPC 104, 106 (1947), the Commission did not articulate a definition of local distribution facilities.

In Wisconsin-Michigan Power Co. v. Federal Power Commission,[51] the Seventh Circuit held that a utility was a jurisdictional public utility where it operated two divisions in Wisconsin and Michigan in a coordinated manner such that electric energy from one state was transmitted to the other, and vice versa, "in appreciable amounts by the power company and by it commingled with energy generated in the

---

376, 383 (8th Cir. 1966) ("Where a company is in fact a public utility, all wholesale sales for resale in interstate commerce are subject to the provisions of sections 205 and 206 of the (FPA), regardless of the facilities used."). The Eighth Circuit further noted that the section 201(b) exemption applies to a company's status as a public utility and not to the Commission's jurisdiction over sales in interstate commerce for resale. *Id., citing Public Utilities Commission, Colton, infra, and Wisconsin-Michigan, infra.*

[50] *Id.* at p. 536.

[51] 197 F.2d 472 (7th Cir. 1952), cert. denied, 345 U.S. 934 (1953) (*Wisconsin-Michigan*).

two respective districts and then delivered to the [wholesale] customers * * *."[52] The court also rejected the notion that the energy changed its form or character when it was stepped down in voltage before it reached the wholesale purchasers.[53]

The court in Wisconsin-Michigan distinguished between transmission and local distribution by focusing on wholesale sales of electric energy versus retail sales ("local rates") of electric energy. It cited the House Report on the FPA, and characterized the legislative history as follows:

The legislative history, (H.R. Rep. No. 1318), 74th Cong., 1st Sess. pages 7, 8 and 27 (1935), discloses that the Congressional Committee intended that the provisions of the (FPA) should apply to the transmission of electric energy in interstate commerce, i.e., the sale of energy at wholesale in interstate commerce, but not to the retail sale of any such energy in local distribution; that the (FPA) left to the state the authority to fix local rates where the energy is brought in from other states, and that the rate making power of the [FPC] was to be confined to those wholesale transmissions which the Supreme Court had held in (Attleboro) to be beyond the reach of the state. Under that decision, said the committee, the rates **[31,975]** charged in interstate wholesale transactions could not

---

[52] *Id.* at p. 474.

[53] *Id.* ("Obviously the energy thus transmitted in interstate commerce is not changed in form or in character except that the voltage is reduced to an extent consistent with efficient economic management and operation.").

be regulated by the states. It defined a wholesale transaction as the sale of electric energy for resale.[54]

The Seventh Circuit's characterization of the House Report seems to equate transmission of electric energy in interstate commerce with the sale of energy at wholesale in interstate commerce. However, this interpretation is at odds with both the plain words of the statute as well as the language of the House Report, both of which refer to transmission in interstate commerce separately from sales for resale in interstate commerce.[55] In addition, the Senate Report, which the Seventh Circuit did not mention, clearly recognized jurisdiction over all interstate transmission lines, whether or not a sale of energy is carried by those lines.[56]

The Wisconsin-Michigan court also cited analogous natural gas cases, stating that "[t]he question is essentially, when does interstate commerce transportation end and where

---

[54]197 F.2d at p. 476 (emphasis added).

[55]See H.R. Rep. No. 1318 at p. 27. ("Subsection (b) confers jurisdiction upon the Commission over the transmission of electric energy in interstate commerce and the sale of electric energy in wholesale in interstate commerce * * *." emphasis added).

[56]See S. Rep. No. 621 at p. 48 ("Jurisdiction is asserted over all interstate transmission lines whether or not there is a sale of the energy carried by those lines * * *.").

do the local distribution facilities first become operative."[57] The court further stated that:

(U)pon delivery to (the wholesaler) local distribution begins when he resells. His sales and distribution at retail are clearly local in character, and constitute only local distribution; but at no point before delivery to him has been completed, has interstate transmission terminated. In other words, "facilities used in local distribution" means facilities used for making resale and distribution to consumers, jurisdiction over which is left to the states. It was only because of this conclusion that the Supreme Court said, [citation omitted], the Act "cut[s] sharply and cleanly between sales for resale and direct sales for consumptive uses." We think there is no ground for the position that local distribution includes any transmission occurring before the wholesaler who resells at retail is reached.[58]

The Seventh Circuit concluded that the sales for resale were made in interstate commerce; that local distribution had not begun; that the interstate character of the transmission persisted until delivery to the wholesaler; that, up to that point, no local distribution facilities were in operation and that, therefore, the sales were subject to Commission regulation.

---

[57]197 F.2d at p. 477.

[58]*Id.*, citing *FPC v. East Ohio Gas Co.*, 338 U.S. 464 (1950) (East Ohio).

In Federal Power Commission v. Southern California Edison Company (the Colton case),[59] the Supreme Court held that the FPA provides a clear line of demarcation between jurisdictional transactions and non-jurisdictional transactions. However, this case, too, involved bundled sales of electric energy. In the facts of the case, Southern California Edison Company (Edison) admitted that it was a public utility by virtue of owning two interstate transmission lines.[60] At issue was whether its sales of electric energy to the City of Colton, California, for resale to Colton's retail customers, were jurisdictional. Included in the electric energy that Edison sold to Colton was out-of-state electric energy from Hoover Dam.[61] The Commission ruled that the sale to Colton was a sale of electric energy at wholesale in interstate commerce subject to regulation under the FPA.[62] In upholding the Commission, the Court held that Edison's importation of out-

---

[59]376 U.S. 205 (1964) (Colton).

[60]The Supreme Court noted that Edison's status as a public utility did not decide the question of whether the FPC could assert jurisdiction over the rates for the Edison-Colton sale. Id. at p. 208 n.3.

[61]*Id.* at p. 208, 209 & n.5.

[62]*Id.* at p. 208. *See Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, 461 U.S. 375, 380 (1983) ("(Colton) held, among other things, that * * * a California utility that received some of its power from out-of-state was subject to federal and not state regulation in its sales of electricity to a California municipality that resold the bulk of the power to others.").

of-state electricity for resale to Colton sufficed to confer federal jurisdiction.

[31,976]

The Court, citing an earlier Supreme Court case,[63] characterized Congressional intent in the FPA:

(W)hat Congress did was to adopt the test developed in the Attleboro line which denied state power to regulate a sale "at wholesale to local distributing companies" and allowed state regulation of a sale at "local retail rates to ultimate consumers."[64]

The Court rejected the argument that FPC jurisdiction was confined to those interstate wholesale sales constitutionally beyond the power of state regulation by force of the Commerce Clause, and was to be determined on a case-by-case analysis of the impact of state regulation upon the national interest. The Court stated that in the FPA:

(C)ongress meant to draw a bright-line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis. This was done in the Power Act by making FPC jurisdiction plenary and extend[ed] it to all wholesale sales in interstate commerce except those

---

[63]*Illinois Natural Gas Co. v. Central Illinois Public Service Co.*, 314 U.S. 498, 504 (1942).

[64]376 U.S. at p. 214.

which Congress has made explicitly subject to regulation by the States.[65]

The Court held that "[t]here is no such exception covering the Edison-Colton sale."[66]

Parties in the Colton case had raised the question of whether jurisdiction over the Colton sale was prevented by the "local distribution" proviso of section 201(b). The Court stated that whether facilities are local distribution facilities is a matter for the Commission to decide in the first instance. Citing CL&P, supra, it stated:

Whether facilities are used in local distribution -- although a limitation on FPC jurisdiction and a legal standard that must be given effect in addition to the technological transmission test * * * -- involves a question of fact to be decided by the FPC as an original matter.[67]

The Court cited evidentiary support and the Commission's expertise in such matters in upholding the Commission's determination that certain facilities owned by Edison were used exclusively to effect the wholesale sale to Colton and not for local distribution. Such facilities included 12 kV lines that served an industrial customer, several lighted highway signs, a residence and a railroad section house before they reached the transformers in the Colton substation. The

---

[65]*Id.* at pp. 215-216.

[66]*Id.* at p. 216 (footnote omitted).

[67]*Id.* at p. 210 n.6 (citation omitted).

FPC had held that those uses prior to the lines reaching the Colton substation did not transform the lines into local distribution facilities.[68]

In Duke Power Company v. Federal Power Commission (Duke),[69] the D.C. Circuit held that a public utility's acquisition of facilities used solely in local distribution, and which would continue to be used for local distribution, was beyond the Commission's jurisdiction under section 203. The case involved Duke Power Company's (Duke's) proposed acquisition of facilities owned by Clemson University (Clemson), which were used to distribute electricity off-campus to customers (primarily university personnel) in two South Carolina counties. Clemson purchased the power at wholesale from Duke. No one appeared to contest the conclusion that the 7 miles of distribution line and 418 service connections owned by Clemson were "local distribution" facilities.[70] Rather, the case turned on interpreting section 203 and whether it was intended to affect only acquisitions of jurisdictional facilities, or also to affect acquisitions of non-jurisdictional facilities. In interpreting section 203, however, the D.C. Circuit extensively analyzed and discussed the fundamental jurisdictional lines that Congress drew in section 201.

---

[68]*Id.* at p. 210 n.6.

[69]401 F.2d 930 (D.C. Cir. 1968) (Duke).

[70]Duke delivered power to Clemson at a distribution voltage of 4,160 volts. The step-down transformers by which the voltage was reduced, and the substations at which the delivery was effected, were owned by Duke. 401 F.2d at p. 931, n.8.

Citing to the CL&P case, the court in Duke stated:

The Act, as we have seen, effectuated federal control over the transmission and the sale at wholesale of electric energy in **[31,977]** interstate commerce, and established the Commission's regulatory power over public utilities engaging in either of these pursuits.[71]

However, quoting CL&P, the court further stated:

The expression "facilities used in local distribution" is one of relative generality. But as used in this Act it is not a meaningless generality in the light of our history and the structure of our government. We hold the phrase to be a limitation on jurisdiction and a legal standard that must be given effect in this case in addition to the technological transmission test.[72]

The court further rejected the Commission's concept that, in order to determine whether jurisdiction over any particular acquisition existed, the impact of local supervision be measured on a case-by-case basis. Quoting from Colton, the court stated:

[T]his "flexible approach" -- involving as it does the consideration, inter alia, of "the effect of the regulation upon the national interest in the commerce" -- has been flatly rejected as a technique for resolving jurisdictional conflicts

---

[71]401 F.2d at pp. 938-39 (emphasis added, footnotes omitted).

[72]*Id.* (footnote omitted).

between the Commission and state bodies * * * We think that like the line "(i)t cut sharply and cleanly between sales for resale and direct sales for consumptive uses" to facilitate jurisdictional determinations in rate regulation, "Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis," in distributing regulatory power over the acquisition of facilities.[73]

The court rejected the Commission's argument that jurisdiction over the merger or consolidation of jurisdictional facilities with those of any other "person" under section 203 gave the Commission jurisdiction over Duke's acquisition. The court stated that the FPA reflects a policy "'that matters largely of a local nature, even though interstate in character, should be handled locally and should receive the consideration of local [officials] familiar with the local conditions in the communities involved.'"[74]

Federal Power Commission v. Florida Power & Light Company[75] is the last major court case to address the Commission's transmission jurisdiction. In this case, the Commission sought to impose its accounting rules upon

---

[73]*Id.* at p. 949 (footnotes omitted).

[74]*Id.* at p. 936 (quoting from Hearings on H.R. 5423 before the House Committee on Interstate and Foreign Commerce, 74th Cong., 1st Sess. 393 (1935) (testimony of then-FPC Commissioner Seavey)).

[75]404 U.S. 453, *reh'g denied*, 405 U.S. 948 (1972) (*Florida Power & Light*).

Florida Power & Light Company (Florida Power & Light). The company's system lay solely within the borders of Florida and did not directly connect with any out- of-state utility.[76] The Commission held that Florida Power & Light did own facilities that transmitted electric energy in interstate commerce, but the Court of Appeals for the Fifth Circuit ruled that the Commission did not have substantial evidence to support its finding.

The Supreme Court reversed. The Supreme Court noted that Florida Power & Light was a member of the Florida Power Pool along with Florida Power Corporation (Florida Power Corp.).[77] In turn, Florida Power Corp. connected with Georgia Power Company (Georgia Power) at a "bus"[78] south of the Georgia-Florida border.[79] Florida Power Corp. regularly exchanged power with Georgia Power.[80] In many instances, Florida Power Corp. transferred power to Florida Power & Light instantly after receiving power from Georgia Power, and transferred power to Georgia Power immediately after receiving power from Florida Power

---

[76]404 U.S. at p. 456.

[77]*Id.* at p. 456.

[78]A "bus" is a connector or group of connectors that serves as a common connection for two or more circuits.

[79]404 U.S. at p. 457.

[80]*Id.*

& Light.[81] The Supreme Court found that power commingled in the bus moved across state lines, and concluded that Florida Power & Light engaged in transmission in interstate commerce. The **[31,978]** Court held that, to establish jurisdiction, the Commission need only show that "some [Florida Power & Light] power goes out of State."[82] The Court further explained that "(i)f any (Florida Power & Light) power has reached Georgia, or (if Florida Power & Light) makes use of any Georgia power * * * FPC jurisdiction will attach * * *."[83]

There is also a line of cases that address, among other things, what constitutes a Commission jurisdictional "sale of electric energy at wholesale"[84] under section 201 of the FPA.[85] These cases all concerned bundled sales. While the issues posed above involve unbundled wheeling, the "resale" cases are helpful to the extent they suggest that local distribution takes place only after power is subdivided. See, e.g., 345 U.S. at 316 ("the facilities supplied 'local

---

[81]*Id.* at p. 457 & n.8.

[82]*Id.* at p. 461. (emphasis omitted).

[83]*Id.* at p. 461 n.10. (emphasis added).

[84]See Section 201(d), 16 U.S.C. §824(d) (1988).

[85]*Public Utilities Commissio*n, supra note 345; *City of Oakland, California v. FERC*, 754 F.2d 1378 (9th Cir. 1985) (*Oakland*). *See also Alexander v. FERC*, 609 F.2d 543 (D.C. Cir. 1979) (*Alexander*).

distribution' only after the current was subdivided for individual consumers.").

4. Natural Gas Act

The Natural Gas Act (NGA) was adopted in 1938. Like the FPA, the NGA contains language limiting the Commission's jurisdiction in situations involving local distribution.[86]

Section 1(b) of the NGA provides:

The provisions of this Act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural.[87]

There is similarity in many respects between the House and Senate Reports on the FPA and the NGA with respect to the jurisdiction given the Commission. For example, all four reports mention Attleboro as placing interstate wholesale transactions beyond the reach of the

---

[86]Courts often rely on cases construing the NGA when interpreting the FPA, and vice versa. *E.g., Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981).

[87]15 U.S.C. §717(b) (emphasis added).

States. As indicated in the House Report on the NGA, the States could "regulate sales to consumers even though such sales are in interstate commerce, such sales being considered local in character and in the absence of congressional prohibition subject to State regulation." (See H.R. Rep. No. 709, 75th Cong., 1st Sess. 1). However, the House and Senate Reports on the NGA contain identical language not found in the reports on the FPA:

In view of the importance of section 1(b), which states the scope of the act, it seems advisable to comment on certain provisions appearing therein. It will be noted that this subsection of the bill, after affirmatively stating the matters to which the act is to apply, contains a provision specifying what the act is not to apply to, as follows:

But shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

The quoted words are not actually necessary, as the matters specified therein could not be said fairly to be covered by the language affirmatively stating the jurisdiction of the Commission, but similar language was in previous bills, and, rather than invite the contention, however unfounded, that the elimination of the negative language would broaden the scope of the act, the committee has included it in this bill. That part of the negative declaration stating that the act shall not apply to "the local distribution of natural gas" is surplusage by reason of the fact that distribution is made only to consumers in connection with sales, and since no jurisdiction is given to the Commission to regulate sales to consumers the

Commission would have no authority over **[31,979]** distribution, whether or not local in character. (Emphasis added).[88]

As a result of this language it can be argued that Congress considered distribution (and local distribution) only in the context of bundled retail sales of natural gas. In fact, it appears that all of the court cases affirming the states' right to regulate local distribution of gas have involved bundled retail sales. See Panhandle Eastern Pipe Line Co. v. Michigan Public Service Commission, 341 U.S. 329 (1951) (Panhandle). There the Court, in affirming the State of Michigan's right to regulate an interstate pipeline's proposed bundled retail sales of gas to industrial consumers, noted that the pipeline company proposed to lay pipeline in "the streets and alleys of Detroit" and ignored the local distribution company's request for additional gas to meet the increased needs of the industrial consumers. Id. at 333. While the Court based its holding on a state's authority to regulate direct (retail) sales to an end- user, rather than on the basis of the section 1(b) local distribution provision, it also found that the proposed sales were "primarily of local interest" and "emphasized the need for local regulation." Id. Two years before Panhandle, the Supreme Court issued its decision in FPC v. East Ohio Gas Co., 338 U.S. 465 (1949) (East Ohio). East Ohio Gas Company owned and operated a natural gas business wholly within the State of Ohio. The company sold gas only to Ohio customers but most of the gas was transported to Ohio from other states by interstate pipelines.

---

[88]H.R. Rep. No. 709, 75th Cong., 1st Sess. 3 (1937); S. Rep. No. 1162, 75th Cong., 1st Sess. 3 (1937).

These interstate pipelines connected inside Ohio with East Ohio's large high pressure lines. The gas then was transported over 100 miles through East Ohio's system to its local distribution system. East Ohio argued that it was exempt from Commission jurisdiction because all of its facilities were local distribution. The Court disagreed, finding the Commission's jurisdiction extends over the transportation of gas in interstate commerce through high-pressure transmission lines and that distribution did not begin until the point where pressure is reduced and gas enters local mains. The Court stated that: "[w]hat Congress must have meant by 'facilities' for 'local distribution' was equipment for distributing gas among customers within a particular local community, not the high-pressure pipelines transporting the gas to the local mains."[89]

The Commission relied in part on East Ohio's high pressure/low pressure distinction in a recent NGA section 7 certificate case which authorized construction of facilities to bypass the local distribution company.[90] On appeal, the California Commission argued that under section 1(b) it should at least have "jurisdiction over the 'taps, meters and

---

[89]338 U.S. at pp. 469-70.

[90]*See Mojave Pipeline Company*, 35 FERC ¶61,199 (1986), *reh'g denied*, 41 FERC ¶61,040 (1987), *reh'g denied*, 42 FERC ¶61,351 (1988); *see also Mojave Pipeline Company*, 66 FERC ¶61,194 (1994), *reh'g pending*.

other tie-in facilities' that link the pipeline to end users."[91] The court disagreed:

While as a matter of ordinary English 'local distribution' might be understood to encompass any delivery to an end user, that is hardly the only or even more plausible reading. Distribution conjures up receiving a large quantity of some good and parcelling it out among many takers.[92]

After reviewing the report language discussed above, the court also stated:

Insofar as congressional committees spoke to the matter * * * they appear to have viewed distribution as confined to its parcelling out function and (probably) even more narrowly, to parcelling out accompanied by retail sales.[93]

In Cascade Natural Gas Corporation v. FERC, et al. (Cascade), the court affirmed the Commission's authorizing an interstate pipeline under section 7 of the NGA "to construct a tap and meter facility that would allow it to deliver natural gas directly to two industrial consumers **[31,980]**

[91] *See Public Utilities Commission of the State of California v. FERC, et al.*, 900 F.2d 269, 273 (D.C. Cir. 1990) (footnote omitted) (*WyCal*).

[92] *Id.* at p. 276.

[93] *Id.* (emphasis in original).

* * *."[94] To reach the interstate pipeline, the industrials constructed a nine-mile pipeline. Together, the facilities bypassed the local distribution company.[95]

The court rejected arguments that section 1(b) deprived the Commission of jurisdiction holding that:

"Local distribution," as Congress viewed the term, involves two components: the retail sale of natural gas and its local delivery, normally through a network of branch lines designed to supply local consumers.[96]

5. Analysis

a. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to a purchaser who will then re-sell the energy to an end user?

The case law supports the conclusion that any facilities of a public utility used to deliver electric energy in interstate commerce to a wholesale purchaser, whether such facilities are labeled "transmission," "distribution" or "local

[94] 955 F.2d 1412, 1414 (10th Cir. 1992).

[95] Unlike the situation in WyCal where the pipeline made direct sales to end users, in Cascade the pipeline transported gas purchased from third parties. *See Northwest Pipeline Corporation*, 51 FERC ¶61,289 at p. 61,909 (1990).

[96] Cascade, 955 F.2d at p. 1421.

distribution," are subject to the Commission's jurisdiction under sections 205 and 206.

This conclusion is supported by Public Utilities Commission, supra, in which the Supreme Court, in the section of its opinion addressing the section 201(b) local distribution provision, held that local distribution facilities began "only after the current was subdivided for individual consumers."[97] Wisconsin-Michigan, supra, in which the Seventh Circuit held that there is no local distribution until the wholesaler who re-sells at retail is reached, is to like effect.

This conclusion, which results in a "functional" line being drawn to determine Commission jurisdiction, is not only consistent with the case law under section 201, but is also consistent with our interpretation of the line drawn under newly amended FPA sections 211 and 212. As long as electric energy is being sold to a legitimate wholesale purchaser, we believe the Commission has jurisdiction under sections 201, 205, and 206 of the FPA over the public utility's facilities used to deliver electric energy to that purchaser.

b. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier directly to an end user?

In analyzing jurisdiction over unbundled retail wheeling, we believe it is important to distinguish between unbundled wheeling provided by the public utility who

---

[97]345 U.S. at p. 316 (footnote omitted).

previously provided bundled retail service to the end user, and unbundled wheeling provided by other public utilities to the end user. For example, a former bundled retail customer may need unbundled wheeling services from its previous public utility generation supplier, as well as unbundled wheeling from one or more intervening public utilities, in order to reach a distant generation supplier. In this scenario, the Commission believes it would have jurisdiction over all of the facilities used for the unbundled wheeling provided by the intervening public utilities.[98] The more difficult issue is whether some portion of the facilities used to transmit energy from the transmitting utility in closest proximity to the end user (the former supplier of the bundled product) is local distribution facilities. We believe that in most, if not all circumstances, some portion will be local distribution facilities.

The case law is replete with statements that the local distribution provision of section 201 must be given effect. However, the Supreme Court in both CL&P and Colton, supra, has stated that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. Thus, there is no clear case law on a "bright line" between transmission and local distribution. In addition, regardless **[31,981]** of the details of the chain of delivery services necessary to move electric energy from the generator to the end user, in most cases the last public utility in the chain will use facilities that

---

[98]The Commission would not have jurisdiction over the rates for the sale of generation by the distant supplier because the transaction would be a retail sale of electric energy.

historically were considered local distribution facilities. Accordingly, unlike the situation involving unbundled wholesale wheeling, for which the case law clearly supports a "functional" test, the Commission believes the case law and practical realities of a changing industry support an analysis of local distribution facilities based on the facilities' functional as well as technical characteristics.

While it would be preferable to draw an absolutely "bright" line (e.g., based on technical characteristics such as voltage), the Commission does not believe this is required by the case law and, importantly, would not be a workable approach in all cases because of the variety of circumstances that may arise and because utilities themselves classify facilities differently (e.g., one utility may classify a 69 kV facility as transmission; another may classify it as distribution).

Therefore, the Commission is adopting several indicators it will evaluate in determining whether particular facilities are transmission or local distribution in the case of vertically integrated transmission and distribution utilities:[99]

•Local distribution facilities are normally in close proximity to retail customers.

[99]In the case of a distribution-only utility, which is franchised by a State or local government and sells only at retail, all of the circuits (and related wires, transformers, towers, and rights of way) which it owns or operates (regardless of voltage) would be local distribution facilities.

•Local distribution facilities are primarily radial in character.

•Power flows into local distribution systems, it rarely, if ever, flows out.

•When power enters a local distribution system, it is not reconsigned or transported on to some other market.

•Power entering a local distribution system is consumed in a comparatively restricted geographical area.

•Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

•Local distribution systems will be of reduced voltage.[100]

In summary, for unbundled wholesale wheeling the Commission will apply a functional test. The only definitive question will be whether the entity to whom the power is delivered is a lawful wholesaler. For unbundled retail wheeling the Commission will apply a combination functional-technical test that will take into account technical characteristics of the facilities used for the wheeling. The

[100]The Commission has analyzed utilities' filings required by the Commission's regulations. These filings are made on FERC Form No. 1. While there is no uniform breakpoint between transmission and distribution, it appears that utilities account for facilities operated at greater than 30 kV as transmission and that distribution facilities are usually less than 40 kV.

Commission concludes that these tests are consistent with the FPA, its legislative history and the case law discussed above.

Robert C. McDiarmid *
Cynthia S. Bogarad
Peter J. Hopkins
Spiegel & McDiarmid
1350 New York Ave., NW
Washington, D.C. 20005
(202) 829-4000

Counsel for Respondent
Transmission Access Study Group

Charles G. Cole *
David B. Raskin
Alice E. Loughran
Steptoe & Johnson LLP
1330 Connecticut Ave., N.W.
Washington, D.C. 20036
(202) 429-6270

Counsel for Respondent
Edison Electric Institute

* COUNSEL OF RECORD

Supreme Court, U.S.
FILED
JUN 18 2001
CLERK

(22) (19)

Nos. 00-568 and 00-809

In The

Supreme Court of the United States

People of the State of New York and the Public Service Commission of the State of New York, et al.
Petitioners,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

Enron Power Marketing, Inc.,
Petitioner,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

JOINT APPENDIX (Vol. 2 of 2)

Louis R. Cohen *
Wilmer, Cutler & Pickering
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000
For Petitioner/Respondent, Enron Power Mkt., Inc.

Lawrence G. Malone *
Public Service Commission
of the State of New York
Three Empire State Plaza
Albany, NY 12223-1350
(518) 474-2510
For Petitioners, People of the State of New York, et al.

Theodore B. Olson *
Solicitor General
Edwin S. Kneedler
Deputy Solicitor General
Austin C. Schlick
Department of Justice
950 Pennsylvania Ave., N.W.
Room 5259
Washington, D.C. 20530-0001
(202) 514-2217
For Respondent, Federal Energy Regulatory Commission

* COUNSEL OF RECORD

BECKER GALLAGHER LEGAL PUBLISHING, INC.
CINCINNATI, OH 800-890-5001

412 pp

James Bradford Ramsay
General Counsel
Sharla M. Barklind
Associate General Counsel
National Association of
Regulatory Utility Commissioners
1101 Vermont Ave., N.W., Ste. 200
Washington, D.C. 20005
(202) 898-2208

Catherine D. Bedell
General Counsel
Richard Bellak
Associate General Counsel
Florida Public Service
Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850
(850) 413-6092

Alan G. Lance
Attorney General
Donald L. Howell, II
Deputy Attorney General
Idaho Public Utilities
Commission
472 W. Washington Street
P.O. Box 83720
Boise, ID 83720-0074
(208) 334-0312

John J. Farmer, Jr.
Attorney General
State of New Jersey
Helene S. Wallenstein
Sr. Deputy Attorney General
Attorney for New Jersey Board
of Public Utilities
124 Halsey Street, 5th Floor
P.O. Box 45029
Newark, New Jersey 07101
(973) 648-4846

Counsel for Petitioners/Respondents
State Public Service Commissions

William H. Chambliss
General Counsel
C. Meade Browder, Jr.
Attorney
Virginia State Corp. Comm'n
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218
(804) 371-9671

Christine O. Gregoire
Attorney General
William Berggren Collins
Sr. Assistant Attorney General
Robert D. Cedarbaum, Sr. Counsel
(for the Washington Utilities and
Transportation Commission)
P.O. Box 40128
Olympia, WA 98504-0128
(360) 664-1188

Harvey L. Reiter
(for Vermont Dept. of Public Service)
Morrison & Hecker
1150 18th Street, N.W., Ste. 800
Washington, D.C. 20036
(202) 785-9100-

Harry Ivey
(for Wyoming Public Service Comm'n)
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002
(307) 777-7824

Jo Anne Sanford
North Carolina Utilities Comm'n
Robert P. Gruber
Public Staff - North Carolina
Utilities Comm'n
Gisele L. Rankin, Staff Attorney
P.O. Box 29520
Raleigh, NC 27626-0520
(919) 733-2435

(Counsel continued on inside back cover)

TABLE OF CONTENTS

VOLUME I:

Relevant Docket Entries in District of Columbia Circuit . . . . . App. 5

Relevant Docket Entries Before Federal Energy Regulatory Commission . . . . . App. 15

Notice of Proposed Rulemaking - Recovery of Stranded Costs by Public Utilities and Transmitting Utilities in Docket No. RM 94-7-000, 59 Fed Reg. 35,274, 35,283-86; 7/11/94 . . . . . App. 17

Comments of North Carolina Utilities Commission and the Public Staff of the North Carolina Utilities Commission; pp. 1, 2-4, 6-7; 5/10/95 . . . . . App. 34

Order No. 888 Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities; pp. 31,632-31,684; 31,687-31,703; 31,718-31,736; 31,743-31,753; 31,764-31,766; 31,770-31,785; 31,898-31,899; 31,919-31,926; 31,966-31,981; 4/24/96 . . . . . App. 42

VOLUME II:

Part 35 - Filing of Rate Schedules - 61 Fed. Reg. 21692-21695; 5/10/96 . . . . . App. 431

Pennsylvania Public Utility Commission's Petition for Rehearing; pp. 1-2, 18-35; 5/23/96 . . . . . App. 444

Virginia State Corporation Commission's Request for Rehearing; pp. 1, 3-9; 5/24/96 . . . . . App. 467

Motion for Rehearing of the Public Service Commission of the State of New York; pp. 1-22; 5/24/96 . . . . . App. 475

Request of the National Association of Regulatory Utility Commissioners for Rehearing; pp. 1, 4-9; 5/24/96 . . . . . App. 499

Application of the Coalition for a Competitive Electric Market For Reconsideration and Clarification or, in the Alternative, Rehearing; pp. 1, 4-8; 5/24/96 . . . App. 509

Order No. 888-A - Order on Rehearing; pp. 30,172-30,188; 30,200-30,218; 30,255-30,226; 30,278-30,281; 30,334-30,350; 30,402-30,424; 30,503-30,543; 3/4/97 . . . . . App. 517

Brief for the Public Service Commissions of New York, Arkansas and Florida, et al.; pp. 1-20; 30-32; 8/19/99 . . . . . App. 792

Excerpts from Electric Power Flow Research Institute: *A Primer on Electric Power Flow for Economists and Utility Planners*; "Resistance and Ohm's Law" pp. 2-6 - 2-11; "Structures of Utility Systems" pp. 3-1 - 3-2; "Transmission and Distribution" pp. 3-12 - 3-17 . . . . . App. 818

NOTICE

The following documents have been omitted in the printing of this Appendix. These documents may be found in Petitioner Enron Power Marketing, Inc.'s Appendix to its Petition for Writ of Certiorari (00-809) at the following pages:

APPENDIX A:

Judgment of the United States Court of Appeals for the District of Colombia Circuit filed 6/30/00 . . . . . 1a

APPENDIX B:

Opinion of the United States Court of Appeals for the District of Columbia Circuit filed 6/30/00 . . . . . 3a

APPENDIX C:

Order of the United States Court of Appeals for the District of Columbia Circuit filed 8/22/00 . . . . . 123a

APPENDIX F:

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats, & Regs. ¶32,514 (1995) (pertinent portion) 33,047-33,085 . . . . . 553a

APPENDIX G:

Statutory Provisions 645a

APPENDIX H:

List of Parties to the Proceeding 683a

Some may also be found in the Petitioner's People of the State of New York and The Public Service Commission of the State of New York's Appendix to its Petition for Writ of Certiorari (00-568) at the following pages:

APPENDIX A:

Order of United States Court of Appeals for the District of Columbia Circuit filed 8/22/00 . . . . . A-1

APPENDIX B:

Judgment of United States Court of Appeals for the District of Columbia Circuit filed 6/30/00 . . . . . B-1

APPENDIX C:

Opinion of United States Court of Appeals for the District of Columbia Circuit decided 6/30/00 . . . . . C-1

APPENDIX G:

Statutory Provisions Involved G-1

PART 35 - FILING OF RATE SCHEDULES
61 FED. REG. 21692-21695

1. The authority citation for part 35 continues to read as follows:

Authority: 16 U.S.C. 791a-825r, 2501-2645; 31 U.S.C. 9701; 42 U.S.C. 7101-7352,

2. Part 35 is amended by revising§35.15, by redesignating §35.28 as §35.29, and by adding new §§35.26, 35.27, and 35.28 to read as follows:

§35.15 Notices of cancellation or termination

(a) *General rule*. When a rate schedule or part thereof required to be on file with the Commission is proposed to be cancelled or is to terminate by its own terms and no new rate schedule or part thereof is to be filed in its place, each party required to file the schedule shall notify the Commission of the proposed cancellation or termination on the form indicated in §131.53 of this chapter at least sixty days but not more then one hundred-twenty days prior to the date such cancellation or termination is proposed to take effect. A copy of such notice to the Commission shall be duly posted. With such notice each filling party shall submit a statement giving the reasons for the proposed cancellation or termination, and a list of the affected purchasers to whom the notice has been mailed. For good cause shown, the Commission may by order provide that the notice of cancellation or termination shall be effective as of a date prior to the date of filing or prior to the date the filing would became effective in accordance with these rules.

(b) *Applicability*. (1) The provisions of paragraph (a) of this section shall apply to all contracts for unbundled transmission service and all power sale contracts:

(i) Executed prior to July 9,1998; or

(ii) If unexecuted, filed with the Commission prior to July 9, 1996.

(2) Any power sales contract executed on or after July 9, 1996 that is to terminate by its own terms shall not be subject to the provisions of paragraph (a) of this section.

(3) *Notice*. Any public utility providing jurisdictional services under a power sales contract that is not subject to the provisions of paragraph (a) of this section shall notify the Commission of the date of the termination of such contract within 30 days after such termination takes place.

§35.26 Recovery of stranded costs by public utilities and transmitting utilities.

(a) *Purpose*. This section establishes the standards that a public utility or transmitting utility must satisfy in order to recover stranded costs.

(b) *Definitions*.

(1) *Wholesale stranded cost* means any legitimate, prudent and verifiable cost incurred by a public utility or a transmitting utility to provide service to:

(i) A wholesale requirements customer that subsequently becomes, in whole or in part, an unbundled wholesale transmission services customer of such public utility or transmitting utility; or

(ii) A retail customer, or a newly created wholesale power sales customer, that subsequently becomes, in whole or in part, an unbundled wholesale transmission services customer of such public utility or transmitting utility.

(2) *Wholesale requirements customer* means a customer for whom a public utility provides by contract any portion of its bundled wholesale power requirements.

(3) *Wholesale transmission services* has the same meaning as provided in section 3(24) of the Federal Power Act (FPA): the transmission of electric energy sold, or to be sold, at wholesale in interstate commerce.

(4) *Wholesale requirements contract* means a contract under which a public utility or transmitting utility provides any portion of a customer's bundled wholesale power requirements.

(5) *Retail stranded costs* means any legitimate, prudent and verifiable cost incurred by a public utility or transmitting utility to provide service to a retail customer that subsequently becomes, in whole or in part, an unbundled retail transmission services customer of that public utility or transmitting utility.

(6) *Retail transmission services* means the transmission of electric energy sold, or to be sold, in interstate commerce directly to a retail customer.

(7) *New wholesale requirements contract* means any *wholesale requirements* contract extended after July 11, 1994, or extended or renegotiated to be effective after July 11, 1994.

(8) *Existing wholesale requirements* contract means any *wholesale requirements* contract executed on or before July 11, 1994.

(c) *Recovery of wholesale stranded costs*.

(1) *General requirement*. A public utility or transmitting utility will be allowed to seek recovery of wholesale stranded costs only as follows:

(i) No public utility or transmitting utility may seek recovery of wholesale stranded costs if such recovery is explicitly prohibited by a contract or settlement agreement, or by any power sales or transmission rate schedule or tariff.

(ii) No public utility or transmitting utility may seek recovery of stranded costs associated with a new wholesale requirements contract if such contract does not contain an exit fee or other explicit stranded cost provision.

(iii) If wholesale stranded costs are associated with a new wholesale requirements contract containing an exit fee or other explicit stranded cost provision, and the seller under the contract is a public utility, the public utility may seek recovery of such costs, in accordance with the contract, through rates for electric energy under sections 205-208 of the FPA. The public utility may not seek recovery of such costs through any transmission rate for FPA section 205 or 211 transmission services.

(iv) If wholesale stranded costs are associated with a new wholesale requirements contract, and the seller under the contract is a transmitting utility but not also a public utility, the transmitting utility may not seek an order from the Commission allowing recovery of such costs.

(v) If wholesale stranded costs are associated with an existing wholesale requirements contract, if the seller under such contract is a public utility, and if the contract does not contain an exit fee or other explicit stranded cost provision, the public utility may seek recovery of stranded costs only as follows:

(A) If either party to the contract seeks a stranded cost amendment pursuant to a section 205 or section 208 filing under the FPA made prior to the expiration of the contract, and the Commission accepts or approves an amendment permitting recovery of stranded costs, the public utility may seek recovery of such costs through FPA section 205-206 rates for electric energy.

(B) If the contract is not amended to permit recovery of stranded costs as described in paragraph (c)(1)(v)(A) of this

section, the public utility may file a proposal, prior to the expiration of the contract, to recover stranded costs through FPA section 205-206 or section 211-212 rates for wholesale transmission services to the customer.

(vi) If wholesale stranded costs ere associated with an existing wholesale requirments contract, if the seller under such contract is a transmitting utility but not also a public utility, and if the contract does not contain an exit fee or other explicit stranded cost provision, the transmitting utility may seek recovery of stranded costs through FPA section 211-212 transmission rates.

(vii) If a retail customer becomes a legitimate wholesale transmission customer of a public utility or transmitting utility, *e.g.*, through municipalization, and costs are stranded as a result of the retail-turned-wholesale customer's access to wholesale transmission, the utility may seek recovery of such costs through FPA section 205-206 or section 211-212 rates for wholesale transmission services to that customer.

(2) *Evidentiary demonstration for wholesale stranded cost recovery*. A public utility or transmitting utility seeking to recover wholesale stranded costs in accordance with paragraphs (c)(1)(v)-(vii) of this section must demonstrate that:

(i) It incurred stranded costs on behalf of its wholesale requirements customer or retail customer based on a reasonable expectation that the utility would continue to serve the customer;

(ii) The stranded costs are not more than the customer would have contributed to the utility had the customer remained a wholesale requirements customer of the utility, or, in the case of a retail-turned-wholesale customer, had the customer remained a retail customer of utility; and

(iii) The stranded costs are derived using the following formula: Stranded Cost Obligation -- (Revenue Stream Estimate- Competitive Market Value Estimate) x Length of Obligation (reasonable expectation period),

(3) *Rebuttable presumption*. If a public utility or transmitting utility seeks recovery of wholesale stranded costs associated with an existing wholesale requirements contract, as permitted in paragraph (c)(1) of this section, and the existing wholesale requirements contract contains a notice provision, there will be a rebuttable presumption that the utility had no reasonable expectation of continuing to serve the customer beyond the term of the notice provision.

(4) *Procedure for customer to obtain stranded cost estimate*. A customer under an existing wholesale requirements contract with a public utility seller may obtain from the seller an estimate of the customer's stranded cost obligation if it were to leave the public utility's generation supply system by filing with the public utility a request for an estimate at any time prior to the termination date specified in its contract.

(i) The public utility must provide a response within 30 days of receiving the request. The response must include:

(A) An estimate of the customer's stranded cost obligation based on the formula in paragraph (c)(2)(iii) of this section;

(B) Supporting detail indicating how each element in the formula was derived;

(C) A detailed rationale justifying the basis for the utility's reasonable expectation of continuing to serve the customer beyond the termination date in the contract;

(D) An estimate of the amount of released capacity and associated energy that would result from the customer's departure; and

(E) The utility's proposal for any contract amendment needed to implement the customer's payment of stranded costs.

(ii) If tim customer disagrees with the utility's response, it must respond to the utility within 30 days explaining why it disagrees. If the parties cannot work out a mutually agreeable resolution, they may exercise their rights to Commission resolution under the FPA.

(5) A customer must be given the option to market or broker a portion or all of the capacity and energy associated with any stranded costs claimed by the public utility.

(i) To exercise the option, the customer must so notify the utility in writing no later than 30 days after the public utility files its estimate of stranded costs for the customer with the Commission.

(A) Before marketing or brokering can begin, the utility and customer must execute an agreement identifying, at a minimum, the amount and the price of capacity and associated energy the customer is entitled to schedule, and the duration of the customer's marketing or brokering of such capacity and energy.

(ii) If agreement over marketing or brokering cannot be reached, and the parties see Commission resolution of disputed issues, upon issuance of a Commission order resolving the disputed issues, the customer may reevaluate its decision in paragraph (c)(5)(i) of this section to exercise the marketing or brokering option. The customer must notify the utility in writing within 30 days of issuance of the Commission's order resolving the disputed issued whether the customer will market or broker a portion or all of the capacity and energy associated with stranded costs allowed by the Commission.

(iii) If a customer undertakes the brokering option, and the customer's brokering efforts fail to produce a buyer within 60 days of the date of the brokering agreement entered into between the customer and the utility, the customer shall relinquish all rights to broker the released capacity and associated energy and will pay stranded costs as determined by the formula in paragraph (c)(2)(iii) of this section.

(d) *Recovery of retail stranded costs*.

(1) *General requirement*. A public utility may seek to recover retail stranded costs through rates for retail transmission services only if the state regulatory authority does not have authority under state law to address stranded costs at the time the retail wheeling is required.

(2) *Evidentiary demonstration necessary for retail stranded cost recovery*. A public utility seeking to recover retail stranded costs in accordance with paragraph (d)(1) of this section must demonstrate that:

(i) It incurred stranded costs on behalf of a retail customer that obtains retail wheeling based on a reasonable expectation that the utility would continue to serve the customer; and

(ii) The stranded costs are not more than the customer would have contributed to the utility had the customer remained a retail customer of the utility.

§35.27 Power sales at market-based rates.

(a) Notwithstanding any other requirements, any public utility seeking authorization to engage in sales for resale of electric energy at market-based rates shall not be required to demonstrate any lack of market power in generation with respect to sales from capacity for which construction has commenced on or after July 9, 1996.

(b) Nothing in this part

(1) Shall be construed as preempting or affecting any jurisdiction a state commission or other state authority may have under applicable state and federal law, or

(2) Limits the authority of a state commission in accordance with state and federal law to establish

(i) Competitive procedures for the acquisition of electric energy, including demand-side management, purchased at wholesale, or

(ii) Non-discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

§35.28 Non-discriminatory open access transmission tariff.

(a) *Applicability*. This section applies to any public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce and to any nonpublic utility that seeks voluntary compliance with jurisdictional transmission tariff reciprocity conditions.

(b) *Definitions*.

(1) *Requirements service agreement* means a contract or rate schedule under which a public utility provides any portion of a customer's bundled wholesale power requirements.

(2) *Economy energy coordination agreement* means a contract, or service schedule thereunder, that provides for trading of electric energy on an "if, as require either the seller or the buyer to engage in a particular transaction.

(3) *Non-economy energy coordination agreement* means any non-requirements service agreement, except an economy energy coordination agreement as defined in paragraph (b)(2) of this section.

(c) *Non-discriminatory open access transmission tariffs.*

(1) Every public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce must have on file with the Commission a tariff applicability for transmission services, including ancillary services, over such facilities. Such tariff must be the open access pro forma tariff contained in Order No. 888. FERC Stats. & Regs. ¶31,036 (Final Rule on Open Access and Stranded Costs) or such other open access tariff as may be approved by the Commission consistant with Order No. 888, FERC Stats. & Regs. ¶31,036.

(i) Subject to the exceptions in paragraphs (c)(1)(ii), (c)(1)(iii), and (c)(1)(iv) of this section, the pro forma tariff contained in Order No. 888, FERC Stats. & Regs. ¶31,036, and accompanying rates, must be filed no later than 60 days prior to the data on which a public utility would engage in a sale of electric energy at wholesale in interstate commerce or in the transmission of electric energy in interstate commerce.

(ii) If a public utility owns, controls or operates facilities used for the transmission of electric energy in interstate commerce as of July 9, 1996, it must file the pro forma tariff contained in Order No. 888, FERC Stats. & Regs. ¶31,036, pursuant to section 206 of the FPA and accompanying rates pursuant to section 205 of the FPA, no later than July 9, 1996. However, if a public utility has already filed, or has on file, an open access tariff and accompanying rates as of April 24, 1996, it may, but is not required to, file new rates with its section 206 pro forma tariff filing.

(iii) If a public utility owns, controls or operates transmission facilities used for the transmission of electric energy in interstate commerce as of July 9, 1996, such

facilities are jointly owned with a non-public utility, and the joint ownership contract prohibits transmission service over the facilities to third parties, the public utility with respect to access over the public utility's share of the jointly owned facilities must file no later than December 31, 1996 the pro forma tariff contained in Order No. 888, FERC Stats. & Regs. ¶31,036, pursuant to section 206 of the FPA and accompanying rates pursuant to section 205 of the FPA.

(iv) If a public utility obtains a waiver of the tariff requirement pursuant to paragraph (d) of this section, it does not need to file the pro forma tariff required by this section.

(v) Any public utility that seeks a deviation from the pro forma tariff combined in Order No. 888, FERC Stats. & Regs. ¶31,036, must demonstrate is consistent with the principles of Order No. 888, FERC Stats. & Regs. ¶31,036.

(2) Every public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce, and tat used those facilities to engage in wholesale sales and/or purchases of electric energy, or unbundled retail sales of electric energy, must take transmission service for such sales and/or purchases under the open access tariff filed pursuant to this section.

(i) Subject to the exceptions in paragraphs (c)(2)(ii) and (c)(3)(iv) of this section, this requirement is effective on the date that such public utility engages in a wholesale sale or purchase of electric energy, but no earlier than July 9, 1996.

(ii) For sales of electric energy pursuant to a requirements service agreement executed on or before July 9, 1996, this requirement will not apply unless separately ordered by the Commission. For sales of electric energy pursuant to a bilateral economy energy coordination agreement executed on or before July 9, 1996, this requirement is effective on December 31, 1996. For sales of

electric energy pursuant to a bilateral non-economy energy coordination agreement executed on or before July 9, 1996, this requirement will not apply unless separately ordered by the Commission.

(2) Every public utility that owns, control: or operates facilities used for the transmission of electric energy in interstate commerce, and that is a member of a power pool, public utility holding company, or other multi-lateral trading arrangement or agreement that contains transmission rates, terms or conditions, must file a joint pool-wide or system-wide open access transmission pro forma tariff.

(i) For any power pool, public utility holding company, or other multi-lateral trading arrangement or agreement that contains transmission rates, terms or conditions and that is executed after July 9, 1996, this requirement is effective on the date that transactions begin under the arrangement or agreement.

(ii) For any public utility holding company arrangement or agreement that contains transmission rates, terms or conditions and that is executed on or before July 9, 1996, this requirement is effective July 9, 1996, except for the Central and South West System, which must comply no later than December 31, 1996.

(iii) For any power pool or multilateral arrangement or agreement other than a public utility holding company arrangement or agreement, that contains transmission rates, terms or conditions and that is executed prior to July 9, 1996, this requirement is effective on December 31, 1996.

(iv) A public utility member of a power pool, public utility holding company or other multi-lateral arrangement or agreement that contains transmission rates, terms or conditions and that is executed on or before July 9, 1996 must begin to take service under a joint pool-wide or system-wide

pro forma tariff for wholesale trades among the pool or system members no later than December 31, 1996.

(d) *Waivers*. A public utility subject to the requirements of this seciion and Order No. 889, FERC Stats. & Regs. ¶31,037 (Final Rule on Open Access Same-Time Information System and Standards of Conduct forPublic Utilities) may file a request for waiver of all or part of the requirements of this section, or Part 37 (Open Access Same-Time Information System and Standards of Conduct for Public Utilities), for good cause shown. An application for waiver must be filed either:

(i) No later than July 9, 1996 or

(ii) No later than 60 days prior to the time the public utility would otherwise have to comply with the requirement.

(e) *Non-public utility procedures for tariff reciprocity compliance*.

(1) A non-public utility may submit a transmission tariff and a request for declaratory order that its voluntary transmission tariff meets the requirements of Order No. 888 (Final Rule on Open Access and Stranded Costs).

(i) Any submittal and request for declaratory order submitted by a non-public utility will be provided an NJ (non-jurisdictional) docket designation.

(ii) If the submittal is found to be an accceptable transmission tariff, an applicant in a Federal Power Act (FPA) section 211 case against the non-public utility shall have the burden of proof to show why service under the open access tariff is not sufficient and why a section 211 order should be granted.

(2) A non-public utility may file a request for waiver of all or part of the reciprocity conditions contained in a public utility open access tariff, for good cause shown. An application for waiver may be filed at any time.

PENNSYLVANIA PUBLIC UTILITY COMMISSION'S PETITION FOR REHEARING

[pp. 1-2]

[1]

UNITED STATES OF AMERICA FEDERAL REGULATORY COMMISSION

[May 23, 1996]

Docket Nos. RM95-8-000 and RM94-7-001

Promoting Wholesale Competition	)
Open Access Non-discriminatory	)
Transmission Services by Public	)
Utilities	)
	)
Recovery of Stranded Costs by	)
Public Utilities and Transmitting	)
Utilities	)
	)

PENNSYLVANIA PUBLIC UTILITY COMMISSION
PETITION FOR REHEARING

BEFORE THE FEDERAL ENERGY REGULATORY COMMISSION:

The Pennsylvania Public Utility Commission ("PaPUC") is the state agency responsible for regulating the rates and service for all privately owned distribution companies and utilities providing electric services within the Commonwealth of Pennsylvania. The PaPUC hereby petitions the Federal Energy Regulatory Commission ("Commission"

or "FERC") for rehearing and reconsideration of its Order No. 888 and the related Final Environmental Impact Statement issued in the above-captioned proceeding consistent with 16 U.S.C. §8251. Specifically, the PaPUC is concerned with the following issues:

Open Access Issues

Issue No. 1 The FERC Has Exceeded the Scope of its Statutory Authority by Requiring Generic Unbundling, Open Access, and Comparability Under Order No. 888.

Issue No. 2 The FERC's Curtailment Policy on a Pro-rata Basis Fails to Hold the Native Load Harmless, "to the extent practical," as Required under the Federal Power Act.

[2]

Issue No. 3 The Redefinition of Federal and State Jurisdiction Under the FERC'S Technical/Functional Test and the Seven Indicia of Distribution are contrary to Law and Fact. (See, Order No. 888 Mimeo at pages 401-443, and Appendix G)

* * * * *

[pp. 18-35]

[18]

Issue No. 2 The FERC's Curtailment Policy on a Pro-rata Basis Fails to Hold the Native Load Harmless, "to the extent practical," as Required under the Federal Power Act.

Under Order No. 888, the transmission provider has the discretion to curtail services, whether firm or non-firm, that will substantially relieve a constraint. That curtailment must be made on a non-discriminatory basis, including the transmission provider's own use of the system, and thus by implication service to the native load.Curtailment must be pro-rata. See, Order No. 888 Mimeo page 335.

While many aspects of the curtailment queue set forth in Order No. 888 are logical, this blanket pro-rata curtailment requirement sets up utility native loads for curtailment while regional, wholesale economic transactions continue to take place. While state curtailment priorities in place, there will already have been a curtailment at the regional level affecting the transmission provider's own use of the system. As part of that use must be to serve the native load, those core customers for whom the system was originally built and maintained under the regulatory compact will be impacted. The degree of those impacts will depend upon the extent and duration of the constraint and the time of day, **[19]** season and climatic conditions under which curtailment takes place.

The PaPUC is particularly aware of this problem in light of experience on January 19, 1994, when pro-rata load shedding was initiated by the Pennsylvania-New Jersey-Maryland Interconnection, in part to preserve economic transactions. As a result, core customers in Pennsylvania ranging from neighborhoods to entire municipalities were abruptly left without power during a record cold spell.

Issue No. 3 The Redefinition of Federal and State Jurisdiction Under the FERC's Technical/Functional Test and the Seven Indicia of Distribution are Contrary to Law and Fact. (See, Order No. 888 Mimeo at pages 401-443, and Appendix G)

Summary

While this issue is presented in the order in which it appears in Order No. 888, it is actually the priority issue for the PaPUC. While specific page cites to the Mimeo Order No. 888 will be provided, the PaPUC also offers a summary of this core issue taken from its Comments and Reply Comments to the MegaNOPR.

> At Order No. 888 Mimeo page 432, the FERC asserts that:
>
> The Commission's assertion of jurisdiction is that if retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

Order No. 888, Mimeo at page 432.

The PaPUC is very concerned with respect to the possibility of a "chilling,, of the development of retail

competition given the **[20]** litigation that may attend the FERC's expansive view of jurisdiction over what it terms, "retail transmission,"[18] and "local distribution." The FERC's declaration of jurisdiction over the rates, terms and conditions of retail wheeling service once that service has been ordered or allowed by a state commission creates a powerful disincentive to authorize or to allow retail wheeling. That is inimical to the evolution of a competitive electric industry and threatens to precipitate extensive litigation with respect to jurisdiction.

The FERC's jurisdiction is much more limited than described in Order No. 888. It extends only to wholesale power transmission and transactions. The FERC does not have the authority to order retail wheeling. Further, the PaPUC does not accede to the jurisdictional formula for determining, "interstate transmission," propounded in the NOPR. That formula may be challenged both on engineering and legal grounds.

The PaPUC does not agree, as a matter of law, that the FERC has jurisdiction over what it terms, the rates, terms and conditions of service of unbundled interstate retail transmission service. The PaPUC disagrees with the FERC's

---

[18]Retail transmission services, as defined by the FERC, means the transmission of electric energy sold, or to be sold, in interstate commerce directly to a retail customer. NOPR Mimeo, page 310. PaPUC maintains that unless a state has authorized retail wheeling, there can be no sale of electricity in interstate commerce to a retail customer. Even if retail wheeling is authorized the sale of electricity will, most likely, be a function of intrastate commerce.

claim that the "plain meaning," of the Federal Power Act supports this contention. Just **[21]** because there is nothing in the statute, the legislative history, or the case law to indicate that the FERC's jurisdiction over the rates, terms and conditions of transmission in interstate commerce extends only to wholesale transmission and not to retail transmission, that does not amount to a grant of jurisdiction over what are retail services.

With the exception of a change in customer status caused by municipalization, PaPUC challenges both the FERC's attempt to take jurisdiction over retail wheeling and retail stranded costs cases as well as the concept of, "transmission at retail in interstate commerce," or "retail transmission." If a state has not approved wheeling to retail customers, then there is no legal basis for the transaction even to take place.

With respect to the FERC's analysis of jurisdictional facilities and line-drawing between transmission and distribution plant, the PaPUC agrees that the Federal Power Act and case law supports the conclusion that facilities of a public utility used to deliver electric energy in interstate commerce to a wholesale purchaser are subject to the FERC's jurisdiction. Whether such facilities are labeled "transmission," "distribution" or ,local distribution," makes a great deal of difference, however, as the United States Supreme Court made clear in the key case of Connecticut Light & Power Company v. Federal Power Commission,[19] In that case, the United States Supreme Court interpreted the

---

[19]Id.

Federal Power Act's Section 201(b) local distribution provision, **[22]** effectively dismissing the very sort of, "negative authority," and combined technical-functional arguments for federal jurisdiction made by the FERC throughout the MegaNOPR and Order No. 888.

The FERC proposes technical factors to evaluate whether particular facilities are transmission or local distribution facilities in the case of vertically integrated transmission and distribution utilities. Those seven indicia of distribution are neither accurate nor acceptable measures of local distribution.

The FERC contends at page 282 of the MegaNOPR and page 403 of the order No. 888 Mimeo that there are seven indicia of local distribution. While advancing the offer of deference to state determinations of what constitutes distribution, the FERC requires the application of the seven indicia by the states in making those determinations. See, Order No. 888 Mimeo at page 430. PaPUC will list those indicia and explain why they are not acceptable measures of local distribution:

1. Local distribution facilities are normally in close proximity to retail customers.

The definition of, "in close proximity," is manifestly unclear and a fertile ground for litigation. By this indicia, the very retail customers that take service at high voltage from transmission lines might be viewed as rendering those lines local distribution facilities by virtue of their close proximity to a retail customer.

[23]

2. Local distribution facilities are primarily radial in character.

Electric distribution may be "radial in character," because the physics of the system as originally constructed dictated that arrangement. But distribution is not always radial in character, nor do the physics of the system require that the system be radial in character. There is no jurisdictional magic in the radial character of distribution lines. Distribution circuits are often networked or looped with adjacent distribution circuits for reliability and load shifting purposes. On the other hand, distribution lines in rural areas are often radial because the circuits are not in close enough proximity to be looped or networked. In short, the radial character of a distribution system (or the lack of same) is not an indicia of local distribution.

3. Power flows into local distribution systems, it rarely, if ever, flows out.

Again, this is a rather gross oversimplification of an engineering concept. All electric power flows out from generators and into the transmission and distribution systems. This concept is dispositive of nothing, including jurisdictional arguments. Whatever power load a circuit cannot absorb goes elsewhere, i.e. it, "flows out."

[24]

4. When power enters a local distribution system, it is not reconsigned or transported on to some other market.

Nor is power reconsigned or transported on to some other market on the transmission grid. This indicia points up the FERC's fundamental failure to understand the dramatically different physics of the electric transmission system. Unlike gas pipelines, which can be packed with molecules that are directed along a closed system, energy transmission is a function of generator location and power displacement. Electric energy is not consigned or transported. Generation and transmission assets are used to increase capacity in a particular area to accommodate coordinated generation and transmission from other areas. Unlike natural gas, there is simply no way to, "paint" an electron a particular color, and to track it from the west to its ultimate destination in the east. Electrons do not move in that fashion. The FERC is confusing consignment and transportation with energizing the grid.

5. Power entering a local distribution system is consumed in a comparatively restricted geographical area.

Again, this indicia is not dispositive of the jurisdictional question. Ail power is consumed in restricted geographical areas. The electrons leaving a generation plant in Ohio are not the same electrons that arrive in New York.

[25]

6. Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

Meters can be, and often are, installed at many points within the power grid as part of a utility's telemetry system

for monitoring the performance of its system. This indicia does not resolve jurisdictional issues but merely reflects a physical manifestation of economic and reliability requirements.

7. Local distribution systems will be of reduced voltage.

In footnote 396 which refers to this indicia, the FERC states:

> The Commission has analyzed utilities' filings required by the Commission's regulations. These filings are made on FERC Form No. 1. While there is no uniform breakpoint between transmission and distribution, it appears that utilities account for facilities operated at greater than 30 kV as transmission and that distribution facilities are usually less than 40 kV.

This generalization is not helpful in resolving the jurisdictional issue, because local distribution can and does occur at levels both higher and lower than those provided by the FERC. Distribution to light industry can occur at 69 kY. Advances in the state of the art now allow a retail residential single phase customer to be served directly from a 34 kV line. Twenty-five years ago, this customer would typically have been served from a 4.16 kV distribution circuit. Does the FERC propose to continue to re-draw its jurisdictional line, periodically, based on technological advances?

Note that regardless of what line of case-law the parties follow, whether AGD or CL&P, the FERC itself states in Order No. **[26]** 888 that, ". . . the cases simply do not resolve dispositively these jurisdictional issues when they arise in the context of the market structures and unbundled transactions being contemplated in today's electric industry." Order No. 888 Mimeo at page 429.

Nothing set forth in Order No. 888, save an as yet undefined offer of deference to state authorities which will be discussed below, changes the positions of the FERC or the PaPUC which have been consistent from July, 1994, when the FERC first articulated its new jurisdictional theories in the original Stranded Cost NOPR.[20]

The PaPUC offers its further assessment of the FERC's jurisdictional theory as articulated in Order No. 888.Eligibility to receive unbundled transmission service is not limited to wholesale customers under Order No. 888. The FERC contends: "It is irrelevant to the Commission's jurisdiction whether the customer receiving the unbundled transmission service in interstate commerce is a wholesale or retail customer." See, Order No. 888 Mimeo page 157.Given the fundamental disagreement with the FERC's jurisdictional theories as finalized in Order No. 888, this contention cannot be allowed to stand. To the PaPUC, it is quite relevant whether a customer is receiving wholesale or retail service. Redefining transmission and distribution service as the FERC

[20]F.E.R.C. Docket No. RM94-7-000, Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, 67 F.E.R.C. ¶61,394 (1994).

does in Order No. 888 does not automatically convey jurisdiction to the FERC, particularly as that redefinition is **[27]** based on an approach specifically rejected by the United States Supreme Court in Connecticut Light & Power Company v. Federal Power Commission.[21]

The PaPUC disagrees as a matter of law with the FERC's assertion that the FERC has exclusive jurisdiction over what it has defined as, "retail transmission." See, Order No. 888 Mimeo page 401. The FERC is impermissibly attempting to expand its jurisdiction, not by virtue of new statutory authority, but by an impermissibly broad and technically insupportable re-definition of existing statutory authority. If it was the intent of Congress to do something so substantial as to redefine and to restructure the electric industry as is argued by the FERC, that intent would be explicit and would not have to be interpreted. In this respect, witness the hearings held before both the U.S. House Energy and Power Subcommittee and the U.S. Senate Energy and Natural Resources Committee thus far on 1996. Those hearings have repeatedly raised the question, both expressly and impliedly, as to whether the FERC has the requisite statutory authority to restructure the electric industry. If the Congress, which the FERC consistently points to as having mandated industry restructuring, must ask such questions then it is questionable whether the FERC's interpretation of the scope of the Energy Policy Act Amendments and the will of Congress is correct.

[21]324 U.S. 515, 65 S.Ct. 749, 89 L.Ed. 1150 (1945).

The PaPUC questions the seven indicia of distribution proposed by the FERC on the basis of both fact and law as stated, above. **[28]** See, Order No. 888 Mimeo page 403.

The PaPUC questions as a matter of law the FERC's definition of the, "traditional tasks of state and federal regulators." See, Order No. 888 Mimeo pages 428-429, See also, fn 541 at p. 431, fn. 544 at p. 435. At the heart of this issue is a fundamental difference with respect to the interpretation of Section 201(b) of the Federal Power Act, the Supremacy Clause, and the X Amendment of the United States Constitution.

FERC Deference to the States

The PaPUC requests clarification of the concept of deference to the states in the definition of local distribution services as first articulated in Order No. 888. The FERC announces this deference at several points in the order, but the FERC does not clarify what a state regulatory agency must demonstrate to secure deference. Further, the FERC offers utilities the opportunity to initiate jurisdictional determinations, by the FERC, regardless of what a state might do. It is only required that a utility first, "consult," with a state prior to coming to the FERC for a jurisdictional determination, and the nature of that, "consultation," is undefined. The language of Order No. 888 also poses a problem for those states contemplating retail wheeling in that deference requires the application of the seven indicia of distribution and conclusions consistent with the findings of Order No. 888:

[29]

> Determining where to draw the jurisdictional line for facilities used in unbundled retail wheeling transactions will involve case-specific determinations that evaluate the seven local distribution indicators that we are adopting. We believe that the Commission should take advantage of state regulatory authorities' knowledge and expertise concerning the facilities of the utilities that they regulate. Therefore, in instances of unbundled retail wheeling that occurs as a result of a state retail access program, we will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[[548] Footnote in Order No. 888] Moreover, we recognize that in some cases the Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by

---

[548]In order to give such deference, we expect state regulators to specifically evaluate the seven indicators and any other relevant facts and to make recommendations consistent with the essential elements of the Rule.

> states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

Order 888 Mimeo at pages 438-439.

This deference provision appears, on its face, only to grant deference in those cases where a state implements the FERC's seven indicia of local distribution and the balance of the open access and comparability portions of the order as stated. Of greater importance to the states are the final two sentences of the quote, above:

[30]

> Moreover, we recognize that in some cases the Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

Order No. 888 Mimeo at page 439.

Note well that variations from the seven indicia of distribution are not deferred to; they are subject to the FERC's consideration. This is a critical distinction that requires elaboration by the FERC.

Given the crucial difference between, "deference" and "consideration," it is clear that under Order No. 888 any state

that authorizes or allows retail wheeling faces the risk of attempted federal preemption by the FERC. The extent of that risk, and the efficacy of the undefined vehicle for FERC, "consideration" of state jurisdictional recommendations beyond the seven indicia of distribution remain unknown.

FERC Resolution of Jurisdictional Issues Initiated by Utilities

Equally troubling is what might be construed as the FERC's attempt to set itself up as a de facto appellate authority should a utility, "consult" with its state regulator but then go to the FERC for a jurisdictional determination. Carefully consider the following language from Order No. 888:

[31]

> Some commenters have asked the Commission to provide a forum to prevent or resolve disputes over the correct classification of facilities as transmission or local distribution. As a means of facilitating jurisdictional line-drawing, we will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with

> the principles established in the Final Rule, the Commission will defer to such classifications and/or cost allocations. [footnote deleted] We encourage public utilities and their state regulatory authorities to attempt to agree to utility-specific classifications and allocations that the utility may file at the Commission.

Order No. 888 Mimeo at 439-440 (emphasis added)

This section of Order No. 888 appears to leave the door open to utilities to circumvent the statutory authority of state regulators. It is not clear what the FERC will do if a utility's classifications and/or cost allocations are <u>not</u> supported by state regulatory authorities. This must be clarified.

<u>FERC Assertion of Jurisdiction Over the Rates, Terms and Conditions of, "Unbundled Retail Transmission."</u>

In its Comments and Reply Comments to the MegaNOPR, the PaPUC challenged the FERC's assertion of jurisdiction over what it terms, "retail transmission." The FERC has reiterated that jurisdictional claim in Order No. 888. In this area, the FERC also speaks of, "deference" to state regulators:

[32]

> A number of commenters have asked the Commission to defer to state commission recommendations or decisions regarding rates, terms and conditions of unbundled retail transmission in interstate commerce by public utilities. Some have suggested that we set

> broad guidelines for such rates, terms, and conditions, and then allow states to actually implement the guidelines. While the Commission cannot simply turn over its jurisdiction for the states to implement, we understand the concerns raised by many state regulators and believe that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances, as discussed below.
>
> As we determined in the NOPR, when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes - - a transmission component and a local distribution component. The Commission has jurisdiction over facilities used for the local distribution component. [[550] Footnote in Order No. 888] Thus, the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. When this occurs, we will generally expect unbundled retail wheeling customers to take service under the same FERC tariff that applies to wholesale customers. However, if the unbundled retail wheeling occurs as part of

---

[550] As discussed above, even if there were instances where no local distribution <u>facilities</u> are used, we believe states have authority over the <u>service</u> of delivering electric energy to end users.

> a state retail access program, it may be appropriate to have a separate retail transmission tariff [[551] Footnote in Order No. 888] to accommodate the design and special needs of such programs. In such situations, the Commission will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by this Final Rule. In addition, rates must be consistent with our Transmission Pricing Policy Statement, and the guidance herein concerning ancillary **[33]** services. [[552] Footnote in Order No. 888]

Order No. 888 Mimeo at pages 440-441 (emphasis added)

The extent of, "deference" under this statement is undefined and is, perhaps, unknowable outside of specific proceedings. The PaPUC does not accept the FERC's claim of jurisdiction over, "retail transmission," and consequently must challenge the FERC's pronouncement of jurisdiction over the rates, terms and conditions of such service.

---

[551] I.e., the tariff would be different from the tariff that applies to wholesale customers. Such tariff would still be filed with the Commission under FPA section 205.

[552] In applying the principles of the Final Rule to retail transmission tariffs, the Commission clearly cannot order retail wheeling directly to an ultimate consumer. See FPA section 212(h).

Buy-sell Transactions

In the MegaNOPR, the FERC discussed buy-sell transactions as a potential threat to FERC jurisdiction. That discussion is reiterated in Order No. 888:

> A final jurisdictional issue raised in the Open Access NOPR concerns buy-sell transactions. We remain concerned, just as we were with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, we reaffim our conclusion that we have jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. However, we recognize that there is a wide range of programs and transactions that might or might not fall within this category. We will address these on a case-by-case basis.

Order No. 888 at page 442

[34]
Again, there is a potential for a jurisdictional conflict with respect to buy-sell transactions to end users that are retail end users. This is a direct consequence of the FERC's "technical-functional test" for jurisdiction. That test is challenged by the PaPUC on legal and technical grounds as described, above.

Conclusion and Summary of the Jurisdictional Section of Order No. 888

The PaPUC renews its objection to the jurisdictional theories of the FERC as summarized at pages 442-443 of Order No. 888:

> In summary, the Commission reaffirms and clarifies its prior jurisdictional conclusions and tests for determining the demarcation between federal and state jurisdiction over transmission in interstate commerce and local distribution. We have attempted to address these issues in a way that provides for flexibility and recognition of legitimate state concerns. With regard to retail services, we recognize the states' concerns that the unbundling of retail transactions would result in changes from what historically has been regulated by the states (principally, the rates of transmission assets previously included in retail rate base). However, the decision to provide unbundled retail wheeling is not the Commission's to make because we have no authority to order transmission directly to an ultimate consumer. In addition, even if a retail access program occurs, we do not believe the unbundling of retail transactions will radically change fundamental state authorities, including authority to regulate the vast majority of generation asset costs, the siting and maintenance of generation facilities and transmission lines, and decisions regarding

> retail service territories. Further, the Commission intends to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies. As the electric industry and state regulatory authorities continue to develop new competitive market structures and consider retail wheeling programs, we believe that the tests and mechanisms we have provided in this Rule will accommodate both Federal and state interests and will help provide jurisdictional certainty to market participants.

[35]
Order No. 888 Mimeo at pages 442-443 (emphasis added)

The PaPUC views with concern the tacit admission by the FERC that assets previously included in retail rate base will be effectively removed from that rate base by virtue of the FERC's re-definition of, "transmission." As those assets were, most likely, previously reviewed and approved by state regulators and form an intrinsic part of state-jurisdictional utility rate base, it is unacceptable for the FERC unilaterally to attempt to wrest jurisdiction from the states. Whether or not one agrees with the regulatory compact and traditional rate-making, the fact remains that the transmission assets previously included (and still included) in retail ratebase are in that rate base as a result of statute. FERC can point to no law that allows it to take jurisdiction of these assets. The inherent and historic nature and use of these facilities by state jurisdictional utilities and their core retail customers virtually

compels state defense of its jurisdiction lest the core of that jurisdiction be undermined.

REQUEST OF THE STAFF OF THE VIRGINIA STATE CORPORATION COMMISSION FOR REHEARING

[p. 1]

United States of America
Federal Energy Regulatory Commission

Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities	)
Recovery of Stranded Costs by Public Utilities and Transmitting Utilities	)

Docket Nos. RM95-8-001 and RM94-7-002

REQUEST OF THE STAFF OF THE VIRGINIA STATE CORPORATION COMMISSION FOR REHEARING

The Staff of the Virginia State Corporation Commission ("VSCC Staff"), pursuant to Rule 713 of the commission's Rules of Practice and Procedure, 18 C.F.R. 385.713, hereby requests rehearing of the Commission's Order No. 888 issued in the above-captioned proceeding on April 24, 1996. Order 888 is unlawful or improper for the following reasons:

1. FERC exceeded the scope of its statutory authority by requiring generic industry-wide unbundling, open access, and comparability.

2. FERC's finding of industry-wide undue discrimination is not supported by the record.

3. FERC's assertion of jurisdiction over the rates, terms and conditions of unbundled retail transmission services is contrary to law.

4. FERC's assertion of jurisdiction over stranded costs related to retail wheeling is contrary to law.

5. FERC's assertion of jurisdiction over stranded costs from retail-turned-wholesale customers is contrary to law.

* * * * *

[pp. 3-9]

[3]

3. FERC's assertion of jurisdiction over the rates, terms and conditions of unbundled retail transmission services is contrary to law.

In Order 888, FERC asserts that "it has exclusive jurisdiction over unbundled retail transmission in interstate commerce by public utilities." FERC also asserts that "it is irrelevant to the Commission's jurisdiction whether the customer receiving the unbundled transmission service in interstate commerce is a wholesale or retail customer." However, FERC cannot point to any specific legal authorization for such jurisdiction, and in fact admits that the law is not clear on this issue. This ambiguity should not be resolved in favor of expanding FERC's jurisdiction.

VSCC Staff agrees with FERC that the law is not dispositive on the question of unbundled retail transmission services. Section 201(a) of the FPA gives FERC **[4]** jurisdiction over ". . . the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce." Cases interpreting the FPA have not addressed the question of whether FERC's jurisdiction over transmission extends to retail customers.[1] However, one court expressly applied the wholesale versus retail distinction to distinguish transmission and local distribution.[2] FERC should apply the wholesale versus retail analysis to the question of unbundled retail transmission.

The legislative history of the FPA does not resolve this jurisdictional question and it provides little support for FERC's conclusion that the act of unbundling generation from delivery shifts jurisdiction from a state to FERC. If anything, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services. When Congress enacted the Energy Policy Act of 1992 (EPAct"), it reaffirmed the wholesale/retail distinction. It amended Section 212 of the FPA to prohibit FERC from issuing orders that require transmission of electric energy to a retail consumer, or that are otherwise inconsistent with state-regulated retail marketing

---

[1] Jersey Central Power & Light Co. V. FPC, 319 U.S. 61 (1943); FPC v. Southern California Edison Co., 3876 U.S. 205 (1964); Arkansas Electric Cooperative Corp. V. Arkansas Public Service Commission, 461 U.S. 375 (1983).

[2] Wisconsin-Michigan Power Co. V. FPC, 197 F.2d 472 (7th Cir. 1952), cert. denied, 345 U.S. 934 (1953).

areas of electric utilities. Further, Section 212(h) of the EPAct includes a provision protecting state authority "concerning the transmission of electric energy directly to an ultimate consumer" from interference by FERC's newly-expanded authority to order wholesale transmission services.

FERC should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer are subject to state jurisdiction, regardless of **[5]** the identity of the party generating or reselling the power or the facilities used to transport the power. This clarification of jurisdiction over delivery of third-party power to an end-user would promote FERC's competitive goals, and it would facilitate state retail wheeling programs that would have otherwise been hindered by Order 888's jurisdictional uncertainty.

4. FERC's assertion of jurisdiction over stranded costs related to retail wheeling is contrary to law.

A state, not FERC, has exclusive jurisdiction over any costs incurred on behalf of a retail customer. In Order 888, FERC asserts that a retail customer who leaves its native utility and takes retail service from an alternative supplier has crossed into the threshold of FERC jurisdiction. This has no basis in law, given the clear restriction on FERC's jurisdiction set forth in the FPA. Section 201(b)(1) restricts FERC's jurisdiction to wholesale sales, and explicitly excludes "any other sale of electric energy." A departing retail customer remains a retail customer, regardless of supplier. No portion of the transaction is a wholesale sale, and there are no wholesale costs associated with a retail

wheeling transaction. Therefore, FERC has no valid claim to address stranded costs arising from retail wheeling.

5. FERC's assertion of jurisdiction over stranded costs from retail-turned-wholesale customers is contrary to law.

Like its assertion of jurisdiction over stranded costs related to retail wheeling, FERC asserts that stranded costs arising from retail-turned-wholesale transactions are subject to FERC's jurisdiction. A change in a customer's status from retail to wholesale (e.g. through municipalization) does not change the status of historical costs. Costs **[6]** incurred on behalf of retail customers are subject to state jurisdiction. Whether a retail customer becomes a retail or wholesale customer of another utility is irrelevant for jurisdictional purposes. Any stranded costs associated with either transaction are costs incurred on behalf of a retail customer. The costs cannot be considered wholesale or transmission (thus FERC-jurisdictional) costs. Thus, there is no legal basis for FERC jurisdiction.

6. The reservation and curtailment priorities in the pro forma tariff fail to protect native load customers, who have paid for the existing transmission system.

Order 888 does not adequately protect native load customers. Native load customers have paid a large portion of the costs of the existing transmission system, and they have endured the environmental and aesthetic impacts associated with transmission lines. They depend on the utility, and unreliable service harms them. Native load customers should

be first in line to receive reserved transmission capacity and last in line to be curtailed in the event of a system constraint. The reservation and curtailment priorities established in Order 888 provide inadequate protection to native load. There are ambiguities in the Order that could be resolved in favor of economic transactions, to the detriment of native load.

A. Reservation Priority

Reservation priority establishes the order in which customers can obtain service. Order 888 allows utilities to reserve existing transmission capacity needed for native load growth and network load growth reasonably forecasted within the utility's current planning horizon. Any capacity reserved for future growth that is not currently needed **[7]** must be posted on the OASIS and made available to others until it is actually needed and used. Further, the Order gives existing firm customers a right of first refusal to existing capacity beyond the terms of their contracts, if they match the rate and contract length offered by another potential customer.

The Order gives native load customers some assurance that they will be entitled to receive service and that sufficient capacity will be reserved for them. However, forecasting load growth and calculating the amount of available transmission capability ("ATC") will be imprecise, at best. Forecasts of transmission load growth are more uncertain than forecasts for generation-related capacity requirements because such forecasts must predict where electrical demands will occur in addition to the magnitude of those loads. Calculations of ATC will be subject to uncertainties associated with load growth, load factors, generating unit availabilities, generating unit additions and retirements, economic

conditions, anomalies in weather, and numerous other factors. Further, in the past, utilities cooperated readily in transmission planning and construction. Under FERC's scheme, they will potentially be competitors and will be less likely to disclose their plans to each other. It will be very difficult, if not impossible, to determine the actual ACT on the transmission grid over both the long and short terms. Further complicating matters is the fact that FERC did not establish any specific method for calculating ATC, and instead will require utilities to file their own methods for calculating ATC.

The possibility that non-native customers could reserve capacity over the economic and reliability needs of native load customers is similar to problems associated **[8]** with the avoided costs provisions of PURPA, where third party power producers were able to enter into long-term purchased power contracts that were based on projections of needed capacity and energy prices. Those projections sometimes resulted in expensive above-market contracts that adversely affected native load customers. Undue reliance on projections has also resulted in uneconomic utility projects. While some reliance on forecasts is a necessity, locking in native load capacity based on imprecise forecasts (and subsequent calculations of ACT) represents a serious and unwarranted risk. Forecasting errors will occur, but native load should not have to bear the burden of these errors.

The Order does not address what will happen if a utility's forecast is too low, and this issue requires clarification. Will native load be entitled to receive sufficient capacity, even though the actual growth exceeded the forecast? Will the calculation of ATC reflect the actual

growth in native load instead of the forecasted growth? Can a utility resell capacity (not reserved for native load because of a low forecast) that is ultimately needed for native load? Is there a fallback mechanism to protect native load customers from a utility's unreasonable forecasts?

Reservation priority must protect native load and give utilities flexibility. The Order should require utilities to reserve sufficient capacity to serve the current and projected needs of native load customers, the wholesale and retail customers on whose behalf the present transmission system was built. The definition of native load customers in Section 1.19 of the tariff should explicitly include existing distribution cooperatives and others who currently provide serve to end users (e.g. municipally-owned utilities). FERC should establish the following reservation priority: native load customers, **[9]** followed by firm contract customers, and last, non-firm customers. FERC should emphasize that the calculation of ATC must not include any capacity that may be needed by native load customers.

MOTION FOR REHEARING OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

[pp.1-22]

[1]

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

[Filed May 24, 1996]

Docket Nos. RM95-8-001 and RM94-7-002

Promoting Wholesale Competition	)
Through Open Access	)
Non-discriminatory Transmission	)
Services by Public Utilities	)
	)
Recovery of Stranded Costs by	)
Public Utilities and	)
Transmitting Utilities	)
	)

MOTION FOR REHEARING OF THE
PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK

PRELIMINARY STATEMENT

The recent issuance by the Federal Energy Regulatory Commission ("FERC" or "Commission") of Order Nos. 888 and 889 lays the foundation for a new era of competition in the electric industry by opening access to electric transmission

systems nationwide. This week, the Public Service Commission of the State of New York ("PSCNY") built on this foundation by declaring its intention to open the state's seven investor-owned electric utilities and the integrated New York Power Pool to wholesale competition in 1997 and to retail access by all classes of electric customers in 1998.[1] These actions make cooperative federalism a reality by bringing the benefits of competition to electric ratepayers in New York State and across the nation. Competition in the generation and energy service **[2]** businesses will lower rates and increase choice of electric providers and innovative energy services.

Accomplishing the shared goal of promoting open access and competition, however, cannot alter the Jurisdictional boundaries between FERC and the states prescribed by Congress in the Federal Power Act. Effective competition must be accomplished by observing the dual Jurisdictional framework, which prescribes that state agencies retain Jurisdiction of retail services, and encourages cooperation between the relevant state and federal administrations. Although the Commission provided deference to state authority in certain areas, FERC Order 888 intrudes on state Jurisdiction in the areas of stranded retail costs and local distribution of electricity. Accordingly, PSCNY moves

---

[1]New York Pub. Serv. Comm'n Case No. 94-E-0952, In the Matter of Competitive Opportunities Regarding Electric Service, Opinion and Order Regarding Competitive Opportunities for Electric Service, Opinion No. 96-12 (issued May 20, 1996).

pursuant to Rule 713 for rehearing of FERC Order 888 as a final agency action.[1]

In Point I, PSCNY requests that FERC declare that it will not backstop state determinations on retail stranded cost recovery. Point II asks FERC to recognize that the states have authority to determine the level of retail-turned-wholesale stranded costs. Point III addresses the fact that, although Order 888 states that FERC will defer to state recommendations on distinguishing transmission from local distribution facilities, the final rules require states to apply the seven factors enunciated in the NOPR, of which PSCNY opposed five in its comments thereon. Hence, **[3]** PSCNY asks the commission to abandon its seven indicator test for distinguishing transmission from local distribution in favor a straightforward functional standard. Finally, although we appreciate the guidance FERC has provided for formation of independent system operators (ISOs) for power pools, the Commission's ISO principles constrain governance options. Point IV, therefore, asks FERC to clarify that it will defer to state-brokered solutions and provide maximum flexibility for creative solutions to assure open access and effective competition in "tight" (integrated) power pools.

By making this motion for rehearing, we do not seek to delay implementation of FERC's final rules. Rather, the PSCNY looks forward to working closely with FERC in implementing state and federal initiatives promoting electric competition. Accordingly, we ask the FERC to modify Order 888 to expedite implementation.

---

[1]16 U.S.C. §8251(a); 18 C.F.R. §385.713(b).

PROCEDURAL HISTORY

On June 29, 1994, the commission issued its original Notice of Proposed Rulemaking on utility stranded costs incurred during the transition to competition in the electric industry.[1] In that NOPR, the commission declared that it had Jurisdiction over rate recovery of utility investments that were stranded due to retail wheeling, and would act as a backstop to state action on retail stranded costs. The PSCNY filed initial comments on **[4]** December 8, 1994 and reply comments on January 24, 1995.[1] In those comments, we stated that "the notion of FERC generally agreeing to act as a backstop to state action, however, could impede state implementation of restructuring programs or transition policies.[2] We further noted that retail stranded costs are a state regulatory concern.

The Commission issued a notice of proposed rulemaking concerning transmission open access and a supplemental notice of proposed rulemaking on stranded cost

---

[1]Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Docket No. RM-94-7-000, 59 Fed. Reg. 35274 (July 11, 1994).

[1]New York State Public Service Comments on the Proposed Rule, Docket No. RM94-7-000 (December 8, 1994); Reply Comments of the New York State Public Service Commission (January 24, 1994).

[2]NYPSC Reply Comments (January 24, 1995), at 2.

recovery on March 29, 1995.[3] Known as the "MegaNOPR", the proposed rulemaking provided, among other things, that: (1) FERC has authority over retail stranded costs and would backstop the states on utility recovery of retail stranded costs, (2) FERC would determine the level, timing and method of recovery of retail-turned-wholesale costs stranded by the creation of new wholesale entities, such as municipal electric utilities, (3) FERC had jurisdiction over transmission facilities, would determine which facilities are transmission and those that were exclusively local **[5]** distribution, and would use a seven-factor test for making that determination.

In our initial comments on the MegaNOPR, the PSCNY argued, among other points, that FERC lacks authority over retail stranded costs, including retail-turned-wholesale costs, and that the NOPR's treatment of local distribution in wholesale power transactions contravenes state authority.[1] In reply comments, we urged FERC to ameliorate the prospect of litigation over retail-turned-wholesale costs by

---

[3]Promoting Wholesale Competition Through Open-Access Non-Discriminatory Transmission Service by Public Utilities, Docket No. RM95-8-000, and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Docket No. RM94-7-001, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, 60 Fed. Reg. 17662 (April 7, 1995).

[1]Comments of the Public Service Commission of the State of New York (August 4, 1995).

allowing the states to determine the level of stranded costs to be recovered in transmission rates.[2]

On April 24, 1996, FERC issued its final rules on transmission open access and stranded cost recovery.[3] FERC Order No. S88 should generally assist the transition to a competitive electric marketplace through the filing by utilities of non-discriminatory open access transmission **[6]** tariffs, the transparent provision of information on wholesale power transactions, and the required unbundling of transmission operation functions from wholesale marketing of electricity. FERC properly noted its deference to the states on several matters, including ordering retail wheeling to ultimate customers, service reliability, generation and transmission siting, local distribution of electricity, and authority to impose

---

[2]Reply Comments of the Public Service Commission of the State of New York. The PSCNY also made presentations at technical conferences convened by FERC on October 27, 1995 regarding the proposed pro forma transmission tariffs and on December 5, 1995 concerning implementation of transmission access in power pools.

[3]Previously, the Commission also issued a notice of proposed rulemaking on information systems. Real-Time Information Networks and Standards of Conduct, Docket No. RM95-9-000, Notice of Proposed Rulemaking, 60 Fed. Reg. 66182 (December 21, 1995). PSCNY filed comments on the RIN NOPR on June 29, 1995. The Commission issued a final rule on the renamed Open Access Same-Time Information System (OASIS) in FERC Order No. 889. 61 Fed. Reg. 21737 (April 24, 1996). In this motion, PSCNY does not seek rehearing of Order No. 889.

non-bypassable retail stranded cost charges. Hence, the Commission stated:

> This Final Rule will not affect or encroach upon stats authority in such traditional areas as the authority over local service issues, including reliability of local service; administration of integrated resource planning and utility buy-side and demand-side decisions, including DSM; authority over utility generation and resource portfolios; and authority to impose non-bypassable distribution or retail stranded cost charges.[1]

Unfortunately, the Commission's final rules intrude on state authority over retail stranded costs, including retail-turned wholesale costs, and state authority over the local distribution of electricity. Moreover, the final rules should be clarified to acknowledge the states' flexibility to broker solutions to transmission access in tight power pools through the implementation of an independent system operator (ISO).

[7]

POINT I
FERC SHOULD DECLARE THAT THE STATES HAVE EXCLUSIVE AUTHORITY OVER RETAIL STRANDED COSTS

---

[1]Id., at 434, n 544.

A. Congress Has Assigned the States Exclusive Jurisdiction Over Retail Stranded Costs

FERC declares in Order 888 that it has jurisdiction over retail stranded costs. The order states:

> We believe that both the Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in order to reach a different generation supplier, and that utilities are entitled, from both a legal and a policy perspective, to an opportunity to recover all of their prudently incurred costs.[1]

The Order further states, however, that FERC will allow utilities to seek federal recovery of stranded costs caused by state-ordered retail wheeling only in limited circumstances. Hence, the Order states that the Commission will address retail stranded cost recovery only when the state regulatory authority does not have authority to address retail stranded costs.[2]

FERC's claim of authority over retail stranded costs contradicts the language of the Federal Power Act. Section 201(a) of the Federal Power Act provides that federal regulation extends to all sales of electric energy in interstate

---

[1]Order 888, at 553.

[2]Id., at 8, 553.

commerce at wholesale except those **[8]** specifically exempted, and would exclude all retail sales. Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205, 211 (1964), reh'g denied, 377 U.S. 913 (1964) (emphasis added). The Supreme court has read Section 201 as drawing "a bright line easily ascertained, between federal and state jurisdiction . . ." 376 U.S. at 215. The Commission's attempt to use its power over wholesale sales to regulate the rate treatment of stranded retail[1] costs violates Congress' assignment of retail regulation to the states. Federal Power Comm'n v. Southern California Edison, 376 U.S. 205 (1964), reh'g denied, 377 U.S. 913 (1964); Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1977), reh'g denied, 405 U.S. 948 (1972); Arkansas **[9]** Electric Cooperative v. Arkansas Public Serv. Comm'n, 461 U.S. 375, 378-80 (1983).[1]

---

[1]If a state utility loses $100 in revenues because a retail customer leaves the company, the fixed costs underlying the $100 remain part of the retail (state) revenue requirement, irrespective of whether the reduced usage resulted from international developments, FERC action, or purely local conditions. That is, the fact that FERC's exercise of its power over wholesale service may have led to the stranding of costs used to serve retail customers would not, in law or logic, move those costs and the revenues supporting them into FERC's jurisdiction. Similarly, if action by state agencies affects wholesale transactions, such effects cannot alter the Jurisdictional boundaries established by Congress.

[1]The Supreme Court has reiterated that the Federal Power Act was intended to leave the states' power over retail sales undisturbed, particularly insofar as it reflected the constitutional division between federal and state power existing when the Federal Power Act was passed. That division was applied to electric utilities

Inasmuch as FERC does not have jurisdiction to determine the rate treatment of costs devoted to retail service, it lacks authority to allow recovery if a state decides not to do so. As the Supreme Court noted in Connecticut Light & Power Co. v. Federal Power Comm'n, 324 U.S. 515 (1945), "the 'insulated chambers of the states' are still laboratories where many lessons in regulation may be learned by trial and error on a small scale without involving a whole national industry in every experiment." 324 U.S. at 530.

FERC's promise to invoke its claimed jurisdiction over retail stranded costs only where states lack authority to addressed stranded costs offers little solace. These statements do not eliminate the possibility that a utility which is unhappy with a state decision on stranded costs might turn to FERC to preempt the states on stranded costs using lack of authority as its pretext.

[10]

On the other hand, if FERC simply intends to provide a forum for retail stranded cost recovery where none exists at

---

in Public Utilities Comm'n of Rhode Island v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927), in which the Supreme Court held that a state regulatory commission could not regulate a wholesale transaction in interstate commerce. Congress filled the resulting gap by establishing federal regulation over wholesale transactions of electric utilities engaged in interstate commerce, but leaving retail intrastate transactions to the states. See Arkansas Electric Cooperative Corp. v. Arkansas Public Serv. Comm'n, 461 U.S. at 378-79 (1983).

the state level,[1] the PSCNY assumes that FERC will leave undisturbed state decisions on retail rate recovery. Consequently, PSCNY respectfully requests FERC to clarify its final rules to declare that it has no intention to review states' decisions on retail stranded investment.

POINT II

FERC SHOULD RECOGNIZE THAT STATES HAVE AUTHORITY TO DETERMINE THE LEVEL OF RETAIL-TURNED-WHOLESALE STRANDED COSTS

A. Congress has Assigned the States Exclusive Jurisdiction over Retail-Turned-Wholesale Stranded Costs

Order 888 asserts that FERC has jurisdiction to determine the rate treatment of costs stranded by the departure of retail-turned-wholesale customers. Moreover, over the dissent of Commissioners' Massey and Hoecker, the Order states that FERC should be the primary forum for addressing the recovery of these utility costs. While federal and state agencies often take actions that affect costs and revenues in each other's jurisdiction, such consequences cannot alter jurisdictional boundaries. Louisiana v. Federal Communications Comm'n, 476 U.S. 355 (1986). In Louisiana v. Federal Communications Comm'n, the **[11]** Supreme Court held that, although the states' setting of depreciation charges

---

[1]It is difficult to envision a circumstance in which a state utility regulatory body has authority to order retail wheeling but lacks jurisdiction to address the rate consequences of its decision.

was alleged to frustrate a federal plan to modernize the telephone network, the Federal Communications Commission's alleged need to rectify the situation did not allow it to infringe on the states' jurisdiction.[1] Again, the Commission's attempt to use its power over transmission or wholesale sales to regulate the rate treatment of stranded retail costs (irrespective of whether the costs at issue were incurred to serve retail customers that became wholesale customers) violates Congress' assignment of retail regulation to the states. Federal Power Comm'n v. Southern California Edison, 376 U.S. 205 (1964), reh'g denied, 377 U.S. 913 (1964); Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1977), reh'g denied, 405 U.S. 948 (1972); Arkansas Electric Cooperative v. Arkansas Public Serv. Comm'n, 461 U.S. 375, 378-80 (1983).

B. FERC Should Modify Order 888 to Leave to the States the Issue of the Level of Stranded Costs to Be Recovered in Transmission Rates

In its Reply Comments on the NOPR, PSCNY offered a cooperative solution to the recovery of retail-turned-wholesale stranded costs. We proposed a process whereby the **[12]** states would set the level of retail-turned-wholesale stranded costs to be recovered in wholesale transmission rates set by FERC. This cooperative method, which was also

[1]Specifically, in rejecting the FCC's claim that state regulation was affecting a federal program, and therefore could be preempted, the Court stressed that allowing the FCC to determine the pace of intrastate depreciation recovery "would be to grant to the agency power to override Congress." (476 U.S. at 374-375).

suggested by a number of state commissions,[1] would respect state interests in controlling the rate impact of stranded costs, while allowing FERC to design the method of cost recovery. Such a mechanism would also address the needs of industrial customers and other stakeholders by providing a forum before state regulators who will be more aware of their particular needs. Accordingly, PSCNY respectfully asks the Commission to modify Order 888 to recognize the states' jurisdiction to determine the level of retail-turned-wholesale costs.

C. FERC's "Reasonable Expectation" Standard Ignores a Series of Criteria Relevant to Retail Stranded Costs

Order 888 states that a utility seeking to recover stranded retail-turned-wholesale costs must show that when it incurred those costs, it had a "reasonable expectation" that the customers would continue to receive bundled retail service.[2] The Commission further states that it will apply the "reasonable expectation standard" to retail stranded cost recovery.[3] Such a test would ignore prudence, customer impact, financial viability and a series **[13]** of criteria traditionally analyzed by regulatory agencies in determining rate treatment of costs incurred with the intention of providing service. See Permian Basis Area Rate Cases, 390 U.S. 747 (1968), reh'g denied sub nom. Bass v. Federal Power

[1]Order No. 888, at 534.

[2]Id., at 572.

[3]Id., at 570-71.

Comm'n, 392 U.S. 917 (1968); Market Street Railway Co. v. Railroad Comm'n of California, 324 U.S. 548 (1945); Jersey Central Power and Lioht Co. v. Federal Energv Regulatorv Comm'n, 810 F.2d 1168 (D.C. Cir. 1987). The PSCNY applies these criteria to arrive at a just and reasonable balancing of consumer and investor interests. N.Y. Pub. Serv. Law S65; Matter of Abrams v. Public Serv. Comm'n, 67 N.Y.2d 205, 215 (1986).

The states are in the best position to determine the nature and level of stranded retail costs. Moreover, decisions by state regulatory agencies on recovery of retail stranded costs will be subject to judicial review under well-established standards in state courts. FERC should let the states decide the rate treatment of retail-turned-wholesale stranded costs.[1]

[14]

POINT III

LOCAL DISTRIBUTION SHOULD BE DISTINGUISHED FROM TRANSMISSION UNDER A FUNCTIONAL STANDARD

FERC's final transmission open access rules are responsive to PSCNY'S comments that the Commission

---

[1]FERC's proposal that stranded costs be administratively determined by a one-time calculation of lost revenues is, in any event, incorrect. If volumes change over, the revenues lost by the migration of a single customer will change, yet the "stranded cost" calculation will not be adjusted.

should respect state authority over local distribution.[1] Order 888 states that the Commission will not encroach upon traditional state authority to regulate the local distribution of electricity.[2] The Commission further states that it will defer to state recommendations in distinguishing local distribution facilities from equipment used for transmission in interstate commerce when states implement retail wheeling of electricity.[3] FERC pronounced that states are free to consider indicators that respect the traditional designation of facilities as transmission versus local distribution.[4] Finally, FERC says that it will respect state authority over the service of delivering electricity to end users, even if that service entails usage of transmission facilities.[5]

PSCNY appreciates FERC'e deference to state authority over local distribution of electricity. Indeed, in our state electric competition proceeding, we have ordered the seven utility members of the New York Power Pool **[15]** to provide information and filings that will assist PSCNY in distinguishing transmission and local distribution facilities in

---

[1]Order 888, at 407.

[2]Id. at 427, 429.

[3]Id. at 429.

[4]Id. at 438.

[5]Id. at 433.

the integrated New York State pool.[1] Nevertheless, we disagree with the Commission's position on two related issues: 1) the Commission's deference should extend to all state commission recommendations regarding the definition of local distribution facilities; and, 2) five of the seven assumptions are inaccurate when applied to large metropolitan areas and to remote rural areas, and should be reexamined.[2]

A. FERC Should Defer in All Instances to the States in Distinguishing Local Distribution from Transmission

Regarding Commission deference to state determinations of what facilities should be considered local distribution, the Commission should not limit its deference to instances in which states order retail wheeling. The question where interstate transmission ends and local distribution begins is arising with increasing frequency. For example, in a pending petition by Suffolk County Electric Agency (SCEA) for transmission service under section 211 of the Federal Power Act, SCEA argues that transmission facilities extend to its customers' meters and, therefore, that there are no state-

---

[1]N.Y.P.S.C. Opinion No. 96-12, supra, at 35, 73 (May 20, 1996).

[2]Comments of the Public Service Commission of the State of New York, August 4, 1995, at 9.

jurisdictional local **[16]** distribution facilities involved.[1] PSCNY opposed SCEA's argument and recommended that FERC defer to our expertise in analyzing local conditions to distinguish distribution facilities from interstate transmission equipment to which a section 211 wheeling order would apply.[2] FERC should modify Order 888 to state that it will defer to state expertise in distinguishing transmission from local distribution facilities.

B. State Agencies and FERC Should Agree on a Definition that Preserves the Traditional Classification of Local Distribution Facilities

1. The Rule's Assumptions Regarding Distribution Facilities Are, In Several Respects, Erroneous

In distinguishing transmission from distribution, Order 888 states that:

> 1. Local distribution facilities are normally in close proximity to retail customers;

---

[1]Suffolk County Electric Agency, Docket No. TX 96-4-000, Application for Order Requiring Transmission Service (January 17, 1996), at 19.

[2]Suffolk County Electric Agency, Docket No. TX 96-4-000, Notice of Intervention by the Public Service Commission of the State of New York (February 21, 1996), at 3-6.

2. Local distribution facilities are primarily radial in character;

3. Power flows into local distribution systems; it rarely, if ever, flows out;

4. When power enters a local distribution system, it is not **[17]** reconsigned or transported on to some other market;

5. Power entering a local distribution system is consumed in a comparatively restricted geographical area;

6. Meters are based at the transmission/local distribution interface to measure flows into the local distribution system;

7. Local distribution systems will be of reduced voltage.[1]

With the exceptions of indicators 3 and 5, these assumptions are not accurate when applied to large metropolitan areas and to remote rural areas.

---

[1]Order 888, at 402.

Concerning the first indicator, local distribution facilities are not necessarily close to retail customers. For example, local distribution lines cover great distances in the New York metropolitan area before voltages are stepped down to consumption levels.

With respect to the second indicator, the rules' assumption that local distribution facilities are primarily radial in character fails to account for network systems. The distribution system for large portions of many metropolitan areas (e.g., New York City, San Francisco) consists of a large grid of loops, referred to as a network system.

Regarding the fourth indicator, reconsignment or transportation of power to different markets can and does occur at the local distribution level. Again, the market **[18]** features of power transactions have little to do with the technical characteristics of local distribution grids.

With respect to the sixth indicator, meters are frequently not part of the transmission/distribution interface, and may also be present at other points in interstate transmission or local distribution systems. The presence of meters is not a discerning characteristic of where interstate transmission ends and local distribution begins.

Concerning the seventh indicator, local distribution systems are not necessarily of reduced voltage. The NOPR had stated that, based on FERC Form No. I filings, transmission facilities appeared to operate at greater than 30

kV and distribution is usually less than 40 kV.[1] That is often not the case in New York State. In rural areas of upstate New York, some lines operating at 23 kV are regarded as transmission lines. By contrast, the New York city metropolitan area operates lines at 69 kV as local distribution facilities. Order 888 did not correct this error.

2. The State/FERC Definition of Distribution Facilities Should Focus on the Functional Characteristics of Local Electric Systems

Only two of the seven technical assumptions adopted by FERC correctly define local distribution. **[19]** Specifically, interstate transmission ends and local distribution begins where: (1) electricity flows into a comparatively restricted geographic area and does not flow back out of that area, and (2) the power is consumed in that area. The Commission should simplify its seven-factor test to this functional measure of local distribution, coupled with the traditional classification of the facilities by the state regulatory body or, in the alternative, what the utility has traditionally classified as distribution. This distinction would be more workable and accurate. Accordingly, FERC should modify Order 888 to adopt the functional standard proposed by PSCNY for distinguishing transmission from local distribution.

---

[1]Open Access NOPR at 285 n. 396.

POINT IV

FERC SHOULD PROVIDE FLEXIBILITY IN THE FORMATION OF INDEPENDENT SYSTEM OPERATORS

Order 888 encourages the formation of independent system operators (ISOs) to assure comparable transmission access in integrated power pools, such as the New York Power Pool. The Commission sets forth eleven principles to guide the formation of ISOs.[1] PSCNY shares FERC's vision that an ISO is the appropriate structure for assuring comparable transmission access where tight power pools exist. An ISO will also ensure safe and reliable service and the infrastructure for effective retail competition in New York. Accordingly, in its order on restructuring the electric industry, PSCNY stated that it expects the seven electric **[20]** and combination utilities and the New York Power Authority to complete a proposal for establishing an ISO for New York by October 1, 1996.[1]

The ISO principles do not provide adequate flexibility for establishing an ISO that will meet New York's needs. For example, in its first principle, FERC states that "The ISO's governance should be structured in a fair and non-discriminatory manner".[2] In interpreting this principle, the

---

[1]Order 888, at 279-86.

[1]N.Y.P.S.C. Opinion No. 96-12, supra, at 35, 73 (May 20, 1996).

[2]Order No. 888, at 280.

commission states that an ISO should be independent of market participants, including control by transmission owners.[3] Accordingly, FERC would apparently reject an ISO proposal that provided for governance by transmission owners.

The parties to New York's electric competition proceeding[4] are discussing formation of an ISO with the following features:

1. Market pricing rules are established by a multi-party board that is not under the control of any one class of market participant;

[21]

2. The establishment and implementation of reliability rules and market rules is handled by a system operator controlled by transmission owners that have divested competitive generation; and,

---

[3] Id.

[4] N.Y.P.S.C. Case 94-E-0951, In the Matter of Competitive Opportunities Regarding Electric Service. The parties to the New York State proceeding have been discussing formation of an ISO for the integrated New York Power Pool for several months. PSCNY has not received or approved any ISO proposal to date.

3. Transmission owners would recover full embedded costs independent of generation dispatch or transmission system operation, so that transmission owners would have no vested interest in decisions on access to, or operation of, the transmission system.

Even though under this proposed model the transmission owners control the system operator, it appears to be consistent with FERC's first ISO principle of fair and non-discriminatory governance because the transmission owners would own no competitive generation. Although the NYPSC has made no decisions on ISO governance, it would not like to see this or other options foreclosed. Consequently, to ensure the formation of an ISO that meets the shared objectives of FERC and PSCNY, the Commission should clarify Order 888 to state that it will allow flexibility to states and utilities in structuring proposals that meet the goals underlying the ISO principles.

CONCLUSION

For the reasons stated above, the Federal Energy Regulatory commission should grant the motion for rehearing of the Public Service Commission of the State of New York **[22]** and modify the final rules contained in order 888 as indicated.

Respectfully submitted,

/s/_____
Maureen O. Helmet
General Counsel
New York State Public
Service Commission
Lawrence G. Malone
Solicitor
Carl F. Patka
Assistant Counsel
Three Empire State Plaza
Albany, New York 12223-1350

DATED: May 24, 1996
Albany, New York

**REQUEST OF THE
NATIONAL ASSOCIATION OF REGULATORY
UTILITY COMMISSIONERS FOR REHEARING**

[p. 1]

**BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION
Washington, D.C.**

[Filed May 24, 1996]

Docket Nos. RM95-8-001 and RM94-7-002

Promoting Wholesale Competition	)
Through Open Access	)
Non-discriminatory Transmission	)
Services by Public Utilities	)
	)
Recovery of Stranded Costs	)
By Public Utilities and	)
Transmitting Utilities	)
	)

**REQUEST OF THE NATIONAL
ASSOCIATION OF REGULATORY UTILITY
COMMISSIONERS FOR REHEARING**

Pursuant to Rule 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §385.713, the National Association of Regulatory Utility Commissioners (NARUC) hereby requests rehearing of Order No. 888 issued by the Federal Energy Regulatory Commission (FERC or the

Commission) in the above-captioned proceeding on April 24, 1996. 60 Fed. Reg. 21540 et seq. (May 10, 1996).

CONCISE STATEMENT OF ALLEGED ERROR

The NARUC respectfully submits that Order No. 888 contains the following errors that should be corrected upon rehearing:

- The Commission's assertion of exclusive jurisdiction over transmission services provided retail consumers on an unbundled basis is inconsistent with the Federal Power Act's allocation of jurisdictional authority between the Commission and the States;

- The Commission's assertion of "primary" authority to provide for the recovery of retail costs of service that are "stranded" when a group of end-users convert to wholesale customers under procedures established in State law exceeds the Commission's authority under the Federal Power Act;

* * * * *

[p. 4-9]

[4]

B. The Commission Should Reverse its Assertion of Jurisdiction over the Rates, Terms and Conditions of Unbundled Retail Transmission Services

In Order No. 888, the Commission restates its conclusion that "it has exclusive jurisdiction over unbundled retail transmission in interstate commerce by public utilities." Slip op. at 400. We respectfully submit that this conclusion is erroneous, and urge its reversal on rehearing for the following reasons.

First, as the Commission notes, the allocation of jurisdiction between the Commission and the States enacted by Congress in both the Federal Power and Natural Gas Acts

> grew out of a market structure in which electricity and transmission generally were bought and sold on a bundled basis. As a result, most transactions included either a retail or wholesale sale of electric energy and jurisdictional lines were drawn on the basis of this sale. Thus, the cases [construing these statutes] simply do not resolve dispositively these jurisdictional issues when they arise in the context of the market structures and unbundled transactions being contemplated in today's electric industry.

Id. at 428 (emphasis added)

Moreover, ambiguous case law is not the only problem in analyzing this jurisdictional question. As the Commission stated in March 1995 in the Notice of Proposed Rulemaking (NOPR) in this docket, the legislative history of the Federal Power Act "does not provide any definitive answers" as well. NOPR at 258.[2]

As NARUC stated in its October 4, 1995 reply comments (at 5-7), we agree with the Commission that the FPA's allocation of jurisdictional responsibility was designed in a far different regulatory era to address a very specific problem: filling the so-called Attleboro gap **[5]** in which States were found incapable of regulating interstate wholesale power sales transactions.[3] We further agree that the case law of that era is not dispositive concerning the question of unbundled retail transmission services either because the cases do not involve the transmission of power to retail customers[4]

---

[2]While including some analysis in the preamble to Order 888, the FERC included as Appendix G to Order No. 888 the bulk of its legal analysis of its exclusive authority over the rates, terms and conditions of unbundled retail transmission. While the Commission believes that the statute is clear on its face as to this issue, it attempts to buttress its analysis by relying on this ambiguous legislative history and out-dated case law.

[3]Public Utilities Commission v. Attleboro Steam & E. Co., 273 U.S. 83 (1927).

[4]Jersey Central Power & Light Co. v. FPC, 319 U.S. 61 (1943); FPC v. Southern California Edison Co., 376 U.S. 205 (1964) (the Colton case); Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission, 461 U.S. 375 (1983).

or fence off local distribution from Federal regulation.[5] As the Commission acknowledged in the NOPR (at 266-8), at least one Court of Appeals, relying on Congress' intent to close the Attleboro gap concerning wholesale power sales, explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services, lending support to NARUC's claim that the Commission should apply the same analysis -- wholesale versus retail -- to the question of unbundled retail transmission.[6]

Second, we agree that the legislative history is not helpful in resolving this jurisdictional question, and provides little support for the Commission's conclusion that the act of unbundling generation from delivery serves to shift jurisdiction from a State commission to the FERC. If anything, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services as the Commission concludes. Indeed, as recently as 1992 when it enacted the Energy Policy Act (EPAct), Congress reaffirmed the wholesale/retail distinction when it amended section 212 of the FPA to prohibit the **[6]** Commission from issuing orders that require transmission of electric energy to a retail consumer, or that are or would be otherwise inconsistent with State-regulated retail marketing areas of electric utilities. §§212(g) and (h). Moreover, in EPAct, Congress included a specific provision protecting State authority "concerning the

---

[5]Connecticut Light & Power Co. v. FPC, 334 U.S. *515* (1945); Duke Power Co. v. FPC, 401 F.2d 930 (D.C. Cir. 1968).

[6]Wisconsin-Michigan Power Co. v. FPC, 197 F.2d 472 (7th Cir. 1952), cert. denied, 345 U.S. 934 (1953).

transmission of electric energy directly to an ultimate consumer" from interference by the Commission's newly-expanded authority to order wholesale transmission services. §212(h).

Third, the seven-factor test that the Commission adopts in Order No. 888 (at 435-6) to apply to the transmission/distribution analysis creates the further difficulty that it does not result in the "bright line" of the sort that the Supreme Court discussed in the Colton case where the wholesale versus retail dichotomy was perhaps most definitively expressed. Rather, the Commission's test necessarily involves a facility-by-facility categorization of utility systems on a company-specific basis, a process hardly consistent with the Court's decision to "mak[e] unnecessary such case-by-case analysis." 376 U.S. at 214.

Accordingly, the NARUC again urges the Commission to adopt on rehearing a test that results in no change in the allocation of jurisdiction between FERC and the States in the retail wheeling/customer choice case from the situation in which electric energy is provided an end user by the utility supplying the delivery service. The Commission should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer is subject to the jurisdiction of the State commission regulating the utility, regardless of the identity of the party generating or reselling the power or the facilities used to transport the power.

[7]

There would be a number of important benefits if this proposal were adopted. First, the Commission would be

implementing a bright line test: delivery of electric energy to an end user would be State-jurisdictional regardless of who generates or supplies the power.[7] As a result, the Court's admonition in Colton against case-by-case analysis as required by Order No. 888 would be heeded. Importantly, a jurisdictional test which focusses on the retail status of the customer receiving the delivery service is entirely consistent with Colton's analysis of wholesale and retail power sales. To the extent that Colton demands a bright-line test as a matter of law, this proposal is one of the few workable and easily understood alternatives, given that under no conceivable analysis can the Commission conclude that the delivery of third-party power to an end user is exclusively FERC-jurisdictional, i.e., never involves a State-jurisdictional distribution component.

Finally, we submit that a decision which definitively clarifies jurisdiction over delivery of third-party power to an end user in the manner we have suggested will actually

---

[7]In, Order No. 888, the Commission appears to conclude that a State-established program allowing for retail customers to choose their source of generation necessarily results in the creation of an unbundled transmission service, and hence effects a shift in jurisdiction from the State commission to the FERC. Slip op. at 430-1. The commission does not address the point we raised in our reply comments as to how the removal of generation serves to unbundle the retail delivery function into separate transmission and distribution services. Id. Without any real explanation, the Commission simply assumes -- erroneously in our view -- that a "resulting transmission transaction" is created when power sale is sold to a retail consumer by someone other than the utility delivering the power.

promote the Commission's competitive goals. While Order No. 888 does provide certain assurances that the Commission will be sensitive to State initiatives, it remains a distinct possibility that States which might consider implementing pro-competitive customer choice programs will be hesitant **[8]** to do so due to their concern that their commissions will be precluded from regulating much (or any) of the retail delivery service provided by the utility.

In sum, the NARUC submits that for sound legal and practical reasons, the Commission should conclude that when a State determines to enable a retail consumer to purchase power from a third-party provider, its State commission retains the authority to regulate the rates, terms and other conditions of the delivery service provided by the utility to that consumer.

C. The Recovery of Retail Stranded Costs, in Either the Retail-turned-Wholesale or Retail Wheeling Case is Subject to the Exclusive Jurisdiction of the States

The NARUC once again respectfully requests that on rehearing, the Commission withdraw that portion of Order No. 888 which provides utilities the opportunity to apply to FERC to recover so-called "retail stranded costs." The Commission lacks the legal authority either to take "primary jurisdiction" in the retail-turned-wholesale case, or to act as a backstop in the retail wheeling case when a State lacks authority to address the issue. Accordingly, FERC must leave the identification, measurement, allocation and recovery of the costs incurred by a utility to serve its retail customers for the State legislatures and commissions to resolve.

Under section 201(a) of the FPA, FERC's jurisdiction is limited to 'the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce," and further, extends "only to those matters which are not subject to regulation by the States." Further, section 201(b) of the statute expressly excludes from the Commission's authority "facilities used for the generation of electric energy" as well as distribution facilities. Costs incurred by a utility to serve its retail customers, whether they be the costs of utility-owned generation facilities, demand-side management programs, "QF" contracts, or so-called **[9]** "regulatory assets," do not involve the sale of electric energy at wholesale nor interstate transmission services, and are therefore not apprehended by the Commission's wholesale sales and transmission jurisdiction. And since both of the scenarios in which FERC is prepared to act to authorize cost recovery (i.e., "municipalization" and retail wheeling) cannot occur without reliance upon the operation of State laws and regulations, it simply cannot be the case that the recovery of retail costs by a utility is "not subject to regulation by the States."

We have not ignored the fact that FERC's jurisdiction under section 201 has been given an expansive construction in judicial opinions issued since the FPA was enacted 60 years ago, nor do we doubt that "electrons do not respect State boundaries." However, even the broadest reading of section 201 cannot provide FERC jurisdiction over unamortized generation (or other) costs held in retail rate base (or otherwise subject to recovery in retail rates) for no other reason than an arguably jurisdictional transmission service provides the Commission a "toll booth" for the recovery of costs that would otherwise be beyond its grasp.

The lack of Commission authority under the FPA to address retail costs applies across the board; however, there are some differences between the two cases (municipalization and retail wheeling) to which we now turn.

APPLICATION OF THE COALITION FOR A COMPETITIVE ELECTRIC MARKET FOR RECONSIDERATION AND CLARIFICATION OR, IN THE ALTERNATIVE, REHEARING

[p. 1]

UNITED STATES OF AMERICA
Before The
FEDERAL ENERGY REGULATORY COMMISSION

[Filed May 24, 1996]

Docket Nos. RM95-8-001 and RM94-7-002

NOTICE OF PROPOSED RULEMAKING REGARDING PROMOTING WHOLESALE COMPETITION THROUGH OPEN ACCESS NON-DISCRIMINATORY TRANSMISSION SERVICES BY PUBLIC UTILITIES

SUPPLEMENTAL NOTICE OF PROPOSED RULEMAKING REGARDING RECOVERY OF STRANDED COSTS BY PUBLIC UTILITIES AND TRANSMITTING UTILITIES

APPLICATION OF THE COALITION FOR A COMPETITIVE ELECTRIC MARKET FOR RECONSIDERATION AND CLARIFICATION OR, IN THE ALTERNATIVE, REHEARING

Jeffrey D. Watkiss
Sam R. Hananel
Tracey L. Bradley
Bracewell & Patterson, L.L.P.
2000 K Street, NW
Fifth Floor
Washington, D.C. 20006-1872

May 24, 1996

* * * * *

[pp. 4-8]

[4]

REQUEST FOR REHEARING

I. DEPARTURES FROM SERVICE COMPARABILITY

A. All Transmission Must Be Unbundled

1. Transmission to retail customers -- The Commission wisely questioned in the underlying notice of proposed rulemaking whether undue discrimination can be eradicated in a "bifurcated" market in which transmission for wholesale is unbundled and transmission for retail is not:

> This will result in service under two separate arrangements -- an explicit wholesale transmission tariff filed at the Commission and an *implicit* retail transmission tariff governed by a state regulatory body. It also raises the possibility that the quality of transmission service for retail purposes will be superior to the quality of transmission service offered for wholesale purposes.

Notice of Proposed Rulemaking Regarding Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities, 60 Fed. Reg. 17,662 at 17,681 (1995) (emphasis added) [hereinafter, "NOPE"]. Despite the Commission's recognition of this risk of service inequality, and its further recognition in the Rule that unbundling transmission from retail service "would be helpful in achieving comparability," Order, 61 Fed. Reg. at 21,577, it fails to require that all transmission service be unbundled from retail services. This failure is arbitrary and irreconcilable with the Commission's concurrent determination in connection with the rules pertaining to stranded-cost recovery that it has jurisdiction over the rates, terms and conditions of **[5]** unbundled interstate transmission services by public utilities to retail customers, and that it has the authority to address retail stranded costs through its jurisdiction over such services. Order. 61 Fed. Reg. at 21,650. Commission jurisdiction over *all* transmission has a solid legal foundation. Because of the manner in which electric power flows, the Supreme Court repeatedly has affirmed that virtually all transmission is in interstate

commerce.[2] Granted, the Commission heretofore has not exercised its Federal Power Act ("FPA") authority to regulate transmission to a retail customer. This does not negate the existence of the Commission's authority.

Perpetuation of a discriminatory dual market, absent *complete* unbundling, finds a clear parallel in the Commission's experience from restructuring the natural gas industry. Following introduction of open-access transportation via Order No. 436, service comparability continued to elude gas markets:

> [T]he firm transportation embedded within the *pipelines' bundled, city-gate, firm sales service is superior* to the pipeline's open-access firm transportation service. This means that pipelines and other gas suppliers are not competing on an even basis for sales customers, even where firm transportation is available to move the gas sold by the pipelines' competitors.

---

[2]*E.g., FPC v. Florida Power & Light Co.*, 404 U.S. 453, 463 (interstate power "commingles in a bus"), *reh'g denied*, 405 U.S. 948 (1972); *FPC v. Southern California Edison Co.*, 376 U.S. 205, 215-16, *reh'g denied*, 377 U.S. 913 (1964); *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 533, 536 (1945); *see also Florida Power & Light Co.*; 29 F.E.R.C. ¶61,140 at 61, 291(1984) ("transportation of power [on] grid . . . used in interstate commerce is subject to this Commission's jurisdiction, even when all the parties to the wheeling transaction are located within the same State").

[6]

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines after Wellhead Decontrol, Order No. 636, 57 Fed. Reg. 13,267 (1992), [Regs. Preambles] III F.E.R.C. Stats. & Regs. ¶30,939 at 30,402 (1992) (emphasis added) [hereinafter "Order No. 636"]. Ultimately, in order to achieve "an even basis for competition," the Commission in Order No. 636 was compelled to unbundle transportation completely, not only from the pipeline's citygate wholesales, but also from the pipeline's direct retail sales. *See* 18 C.F.R. §284:10 (1994) (requiring pipelines to phase in conversion rights for all firm sales service customers whose contracts preceded Order No. 436).

Just as open access *alone* did not uproot inequality between unbundled transportation provided to third-party shippers and the bundled transportation that the pipelines provided to themselves to make citygate sales, the *pro forma* tariffs *alone* cannot establish comparability between the transmission service that a public utility provides to its retail sales functions and the wholesale transmission services that it provides to others. Ineluctably, discrimination will persist until there is total unbundling and consumers *of all* transmission services, wholesale and retail, take service pursuant to the same tariff at posted rates. The Commission's authority *and responsibility* under the FPA to address such discriminatory differences between wholesale and retail markets is well established in the prevailing decisional precedents. *See FPC v. Conway Corp.*, 426 U.S. 271, 273 (1976).

[7]

The failure to unbundle transmission to retail customers is also squarely at odds with the Commission's decisional precedents under the Natural Gas Act CNGA"). In *Mississippi River Transmission Corp. v. FERC,* 969 F.2d 1215 (D.C. Cir. 1992), the court affirmed the Commission's interpretation of NGA section 1 (b), 15 U.S.C. §717(b) (I 988), as authorizing the Commission to regulate the price of transportation service that MET provided in support of certain firm direct sales. In relevant part, NGA section 1 (b) is identical to FPA section 201(b): "The provision of this chapter shall apply to the transportation of natural gas in interstate commerce . . . ." Based on this broad grant of jurisdiction, the court held that:

> FERC is not barred from regulating a pipeline's interstate transportation of natural gas merely because the sale of the gas being transported is not itself subject to federal regulation. FERC's authority over such transactions is beyond dispute.

969 F.2d at I217 (citing *FPC v. East Ohio Gas Co.,* 338 U.S. 464, 468 (1950)); *accord Alabama Tennessee Natural Gas Co.,* 64 F.E.R.C. ¶61,084 at 61,846 (1993); *Carnegie Natural Gas Co.,* 63 F.E.R.C. ¶61,103 at 61,612 (1993). In reaching this conclusion, the court rejected MET's contention that the Commission's NGA §1(b) jurisdiction to regulate the price, terms and conditions of interstate transportation is divested whenever the subject transportation is bundled with

a non-jurisdictional sale.[3] The court found this contention untenable because it would invite manipulation:

[8]

> As far as the statute is concerned, there would be no doubt of FERC's section l(b) authority if MRT, instead of charging a bundled price, had charged separately for the gas itself. To accept MRT's position would therefore be tantamount to conferring on private parties the power to decide whether FERC could set the rate for interstate transportation. Private parties would have this power because it would be entirely up to them whether to structure a direct sale and interstate transportation transaction in terms of a bundled price or separate charges.

Id. at 1218. Just as the Commission's NGA section l(b) jurisdiction to regulate natural gas transportation to retail customers was "beyond dispute" in *Mississippi River,* it is equally beyond dispute that the Commission possesses FPA section 201(b)jurisdiction to unbundle and regulate electricity transmission in interstate commerce to a retail customer.

---

[3]The NGA and the FPA are different with respect to the certificate of public convenience and necessity (" PC&N") that a natural gas company must obtain under NGA §7, 15 U.S.C. §717f(c) (1988), in advance of providing any jurisdictional service. There is no analog to the PC&N process in the FPA. The Commission's §7 jurisdiction over transportation was not contested in *Mississippi River*. *See* 969 F2d at 1217. Rather, only the Commission's authority under §1(b) to regulate the price of gas pipeline transportation to retail customers was at issue.

In sum, there is no rational basis for regulating factually undifferentiated uses of the transmission lines differently. Achieving and policing comparability will require the Commission to go beyond artificial distinctions between wholesale and retail transactions and insist that all transmission providers and customers confront the same unbundled market.

FEDERAL ENERGY REGULATORY COMMISSION
ORDER 888-A

[Issued March 4, 1997]

Docket Nos. RM95-8-0001and RM94-7-002

Order No. 888-A

* * * * *

[pp. 30,172 - 30,182]

[30,172]
62 F.R. 12274 (March 14, 1997)

18 C.F.R. Part 35

Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities

AGENCY: Federal Energy Regulatory Commission.

ACTION: Final rules; order on rehearing.

SUMMARY: The Federal Energy Regulatory Commission (Commission) reaffirms its basic determinations in Order No. 888 and clarifies certain terms. Order No. 888 requires all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce to have on file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service. Order No. 888 also permits public utilities and

transmitting utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and Federal Power Act section 211 transmission services. The Commission's goal is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers.

EFFECTIVE DATE: Changes to Order No. 888 made in this order on rehearing will become effective on [insert date 60 days after date of publication in the *Federal Register*].

FOR FURTHER INFORMATION CONTACT: David D. Withnell (Legal Information -- Docket No. RM95-8-001), Office of the General Counsel, Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-2063

Deborah B. Leahy (Legal Information -- Docket No. RM94-7-002), Office of the General Counsel, Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-2039

Dan T. Hedberg (Technical Information -- Docket No. RM95-8-001), Office of Electric Power Regulation, Federal Energy Regulatory Commission, 888 First Street, N.E. Washington, D.C. 20426, (202) 208-0243

Joseph M. Power (Technical Information -- Docket No. RM94-7-002), Office of Electric Power Regulation, Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426, (202) 208-1242

SUPPLEMENTARY INFORMATION: In addition to publishing the full text of this document in the Federal Register, the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in the Public Reference Room at 888 First Street, N.E., Washington, D.C. 20426.

The Commission Issuance Posting System (CIPS), an electronic bulletin board service, provides access to the texts of formal documents issued by the Commission. CIPS is available at no charge to the user and may be accessed using a personal computer with a modem by dialing 202-208-1397 if dialing locally or 1-800-856-3920 if dialing long distance. To access CIPS, set your communications software to 19200, 14400, 12000, 9600, 7200, 4800, 2400, or 1200 bps, full duplex, **[30,173]** no parity, 8 data bits and 1 stop bit. The full text of this order will be available on CIPS in ASCII and WordPerfect 5.1 format. CIPS user assistance is available at 202-208-2474.

CIPS is also available through the Fed World system. Telnet software is required. To access CIPS via the Internet, point your browser to the URL address: http://www.fedworld.gov and select the "Go to the FedWorld Telnet Site" button. when your Telnet software connects you, log onto the FedWorld system, scroll down and select FedWorld by typing: 1 and at the command line then typing: /go FERC. FedWorld may also be accessed by Telnet at the address fedworld.gov.

Finally, the complete text on diskette in Wordperfect format may be purchased from the Commission's copy

contractor, La Dorn Systems Corporation. La Dorn Systems Corporation is also located in the Public Reference Room at 888 First Street, N.E., Washington, D.C. 20426.

Table of Contents

I. Introduction and Summary
II. Public Reporting Burden
III. Background
IV. Discussion
A. Scope of the Rule
1. Introduction
2. Functional Unbundling
3. Market-based Rates
a. Market-based Rates for New Generation
b. Market-based Rates for Existing Generation
4. Merger Policy
5. Contract Reform
6. Flow-based Contracting and Pricing
B. Legal Authority
C. Comparability
1. Eligibility to Receive Non-discriminatory Open Access Transmission
a. Unbundled Retail Transmission and "Sham Wholesale Transactions"
b. Transmission Providers Taking Service Under Their Tariff
2. Service that Must be Provided by Transmission Provider
3. Who Must Provide Non-discriminatory Open Access Transmission
4. Reservation of Transmission Capacity by Transmission Customers

5. Reservation of Transmission Capacity for Future Use by Utility
6. Capacity Reassignment
7. Information Provided to Transmission Customers
8. Consequences of Functional Unbundling
a. Distribution Function
b. Retail Transmission Service
c. Transmission Provider
1. Taking Service Under the Tariff
2. Accounting Treatment
D. Ancillary Services
1. Specific Ancillary Services
a. Scheduling, System Control and Dispatch Service
b. Reactive Supply and Voltage Control from Generation Sources Service
c. Energy Imbalance Service
(1) Description of Energy Imbalance
(2) Energy Imbalance Bandwidth
2. Ancillary Services Obligations
a. Obligation of a Control Area Utility
b. Obligation to Provide Dynamic Scheduling
c. Obligation As Agent
3. Miscellaneous Ancillary Services Issues
a. Transmission Provider as Ancillary Services Merchant
b. QF Receipt of Ancillary Services
c. Pricing of Ancillary Services
E. Real-Time Information Networks
F. Coordination Arrangements: Power Pools, Public Utility Hoiding Companies, Bilateral Coordination Arrangements, and Independent System Operators
1. Tight Power Pools
2. Loose Pools

3. Public Utility Holding Companies
4. Bilateral Coordination Arrangements

G. *Pro Forma* Tariff

1. Tariff Provisions That Affect The Pricing Mechanism

a. Non-Price Terms and Conditions

[30,174]

b. Network and Point-to-Point Customers' Uses of the System (so called "Headroom")

c. Load Ratio Sharing Allocation Mechanism for Network Service

(1) Multiple Control Area Network Customers

(2) Twelve Monthly Coincident Peak v. Annual System Peak

(3) Load and Generation "Behind the Meter"

(4) Existing Transmission Arrangements associated with Generating Capacity Entitlements (e.g., "preference power" customers of PMAs)

d. Annual System Peak Pricing for Flexible Point-to-Point Service

e. Opportunity Cost Pricing

(1) Recovery of Opportunity Costs

(2) Redispatch Costs

f. Expansion Costs

g. Credit for Customers' Transmission Facilities

h. Ceiling Rate for Non-firm Point-to-Point Service

i. Discounts

j. Other Pricing Related Issues Not Specifically Addressed in the Final Rule

(1) Demand Charge Credits

(2) In-Kind Transactions

2. Priority For Obtaining Service

a. Reservation Priority for Existing Firm Service Customers

b. Reservation Priority for Firm Point-to- Point and Network Service

c. Reservation Priorities for Non-firm Service

3. Curtailment and Interruption Provisions

a. Pro-rata Curtailment Provisions

b. Curtailment and Interruption Provisions for Non-firm Service

4. Reciprocity Provision

5. Liability and Indemnification

6. Umbrella Service Agreements

7. Other Tariff Provisions

a. Minimum and Maximum Service Periods

b. Amount of Designated Network Resources

c. Eligibility Requirements

d. Two-Year Notice of Termination Provision

e. Termination of Service for Failure to Pay Bill

f. Definition of Native Load Customers

g. Off-System Sales

h. Requirements Agreements

i. Use of Distribution Facilities

j. Losses

k. Modification of Non-rate Terms and Conditions

l. Miscellaneous Tariff Modifications

(1) Ancillary Services

(2) Clarification of Accounting Issues

(a) Transmission Provider's Use of Its System (Charging Yourself)

(b) Facilities and System Impact Studies

(c) Ancillary Services

(3) Miscellaneous Clarifications

(a) Electronic Format

(b) Administrative Changes
8. Specific Tariff Provisions
9. Miscellaneous Tariff Administrative Changes
10. Pro Forma Tariff Compliance Filings
H. Implementation
1. Group 1 Public Utilities
2. Group 2 Public Utilities
3. Clarification Regarding Terms and Conditions Reflecting Regional Practices
4. Future Filings
5. Waiver
I. Federal and State Jurisdiction: Transmission/Local Distribution
J. Stranded Costs
1. Justification for Allowing Recovery of Stranded Costs
2. Cajun Electric Power Cooperative, Inc. v. FERC
3. Responsibility for Wholesale Stranded Costs (Whether to Adopt Direct Assignment to Departing Customers)
4. Recovery of Stranded Costs Associated With New Wholesale Requirements Contracts
[30,175]
5. Recovery of Stranded Costs Associated With Existing Wholesale Requirements Contracts
6. Recovery of Stranded Costs Caused by Retail-Turned-Wholesale Customers
7. Recovery of Stranded Costs Caused by Retail Wheeling
8. Evidentiary Demonstration Necessary -- Reasonable Expectation Standard
9. Calculation of Recoverable Stranded Costs

10. Stranded Costs in the Context of Voluntary Restructuring
11. Accounting Treatment for Stranded Costs
12. Definitions, Application, and Summary
K. Other
1. Information Reporting Requirements for Public Utilities
2. Small Utilities
3. Regional Transmission Groups
4. Pacific Northwest
5. Power Marketing Agencies
a. Bonneville Power Administration (BPA)
b. Other Power Marketing Agencies
6. Tennessee Valley Authority
7. Hydroelectric Power
8. Residential Customers
9. Miscellaneous Issues
V. Environmental Statement
A. The Appropriate No-Action Alternative
B. Challenges to Modeling Assumptions
1. Appropriate Base Case
2. Challenge to the Use of Computer Modeling
3. Transmission Assumptions
4. Plant Availabilities and Heat Rates
5. Reserve Margins
6. Northeast MOU
7. Natural Gas Prices
8. Expanded Transmission Analysis
C. Mitigation
D. Emissions Standards Disparity
E. Short-Term Consequences of the Rule
G. Cost Benefit Analysis
H. Socioeconomic Impacts

I. Coastal Zone Management Act
VI. Regulatory Flexibility Act Certification
A. Docket No. RM95-8-000 (Open Access Final Rule)
1. Public Utilities
2. Non-Public Utilities
B. Docket No. RM94-7-000 (Stranded Cost Final Rule)
1. Public Utilities
2. Non-Public Utilities
VII. Information Collection Statement
VIII. Effective Date

I. Introduction and Summary

On April 24, 1996, the Commission issued Final Rules (Order Nos. 888 and 889) intended to remedy undue discrimination in the provision of interstate transmission services by public utilities and to address the stranded costs that may result from the transition to more competitive electricity markets.[1] At the heart of these rules is a requirement that prohibits owners and operators of monopoly transmission facilities from denying transmission access, or

[1]Promoting Wholesale Competition Through Open Access Non- discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, 61 FR 21,540 (May 10, 1996), *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶31,036, *clarified*, 76 FERC ¶61,009 and 76 FERC ¶61,347 (1996). Order No. 889 [*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶31,035], is an accompanying rule and specific rehearing arguments on that rule will be addressed separately.

offering only inferior access, to other power suppliers in order to favor the monopolists' own generation and increase monopoly profits -- at the expense of the nation's electricity consumers and the economy as a whole.

The electric utility industry today is not the industry of ten years ago, or even **[30,176]** five years ago. While historically it was assumed that local utilities would be the only ones to generate and transmit power for their customers, today there is a broad array of potential competitors to supply power and widespread transmission facilities that can carry power vast distances. But competitors cannot reach customers if they cannot have fair access to the transmission wires necessary to reach those customers. It is against this industry backdrop that the Commission in Order No. 888 exercised its public interest responsibilities pursuant to sections 205 and 206 of the Federal Power Act (FPA), to reexamine undue discrimination in interstate transmission services and the effect of that discrimination on the electricity customers whom we are bound to protect under the FPA.

We here reaffirm the legal and policy bases on which Order No. 888 is grounded. Utility practices that were acceptable in past years, if permitted to continue, will smother the fledgling competition in electricity markets and undermine the national policies reflected in the Energy Policy Act of 1992 to encourage the development of competitive markets. We firmly believe that our authorities under the FPA not only permit us to adapt to changing economic realities in the electric industry, but also require us to do so, as necessary to eliminate undue discrimination and protect electricity customers. The record supports our conclusion that, absent open access, undue discrimination will continue to be a fact

of life in today's and tomorrow's electric power markets. As recent events clearly demonstrate, unbundled electric transmission service will be the centerpiece of a freely traded commodity market in electricity in which wholesale customers can shop for competitively-priced power.

The only way to effectuate competitive markets and remedy discrimination is through readily available, non-discriminatory transmission access. The Commission estimates the potential quantitative benefits from such access will be approximately $3.8 to $5.4 billion per year in cost savings, in addition to the non- quantifiable benefits that include better use of existing assets and institutions, new market mechanisms, technical innovation, and less rate distortion.

Order No. 888 has two central components. The first requires all public utilities that own, operate or control interstate transmission facilities to offer network and point-to-point transmission services (and ancillary services) to all eligible buyers and sellers in wholesale bulk power markets, and to take transmission service for their own uses under the same rates, terms and conditions offered to others. In other words, it requires non-discriminatory (comparable) treatment for all eligible users of the monopolists' transmission facilities. The non-discriminatory services required by Order No. 888, known as open access services, are reflected in a pro forma open access tariff contained in the Rule. The Rule also requires functional separation of the utilities' transmission and power marketing functions (also referred to as functional unbundling) and the adoption of an electric transmission system information network.

The second central component of Order No. 888 was to address whether and how utilities will be able to recover costs that could become stranded when wholesale customers use the open access tariffs, or FPA section 211 tariffs,[2] to leave their utilities' power supply systems and shop for power elsewhere. Because of competitive changes occurring at the retail level, as numerous states have begun retail transmission access programs, Order No. 888 also clarifies whether and when the Commission may address stranded costs caused by retail wheeling and the extent of the Commission's jurisdiction over unbundled retail transmission. The Commission further addresses the circumstances under which utilities and their wholesale customers may seek to modify contracts made under the old regulatory regime, taking into account the goals of reasonably accelerating customers' ability to benefit from competitively priced power and at the same time ensuring the financial stability of electric utilities during the transition to competition.

[30,177]

137 entities filed requests for rehearing and/or clarification of Order No. 888. While these parties raise a variety of arguments -- including legal, policy, and technical arguments -- the majority (including a majority of public utilities) agree that we need to harness the benefits that competitive electricity markets can bring to the nation. The

---

[2]Under section 211 of the FPA, the Commission, on a case-by- case basis upon application by an eligible customer, may order both public utilities and non-public utilities that own or operate transmission facilities used for the sale of electric energy at wholesale to provide transmission services to the applicant if it finds it is in the public interest to issue such order.

disagreements primarily focus on the mechanics of how we should do this, who should pay the costs of the transition to competition, and how long the transition should take.

First, parties disagree on what is necessary to remedy undue discrimination and to develop truly competitive wholesale markets. Many focus specifically on the tariff terms and conditions of good transmission access and seek changes in the Order No. 888 pro forma tariff. In response to these types of rehearing arguments, the Commission has fine-tuned or changed some of the pro forma tariff terms and conditions to better ensure that they do not permit discrimination and that they result in well-functioning markets. Other petitioners focus on additional structural changes which they believe are necessary, such as mandatory corporate restructuring (divestiture of generation assets) or mandatory creation of independent transmission system operators (ISOs). With regard to restructuring, the Commission continues to believe that functional unbundling of the utility's business, not corporate divestiture or mandatory ISOs, is sufficient to remedy undue discrimination at this time.

The most contentious arguments raised on rehearing involve how we deal with the transition costs associated with moving to competition. Some utilities have invested millions of dollars in facilities and purchased power contracts based on an explicit or implicit obligation to serve customers and the expectation that those customers would remain on their systems for the foreseeable future. These utilities face so-called "stranded costs" which, if not recovered from the customers that caused the costs to be incurred, could be shifted to other customers.

There are two basic categories of rehearing arguments regarding stranded cost recovery. Most utilities want a guarantee from this Commission that they will recover all stranded costs, whether caused by losing retail customers or wholesale customers. Many customers, on the other hand, want to be able to abrogate existing power supply contracts so that they can immediately leave their current suppliers' systems and shop for cheaper power elsewhere, without paying the sunk costs that their suppliers incurred on their behalf.

In response to these diverse arguments, the Commission has struck a reasonable balance that, for certain defined circumstances, permits utilities the opportunity to seek extra-contractual recovery of stranded costs from their departing customers and permits customers the opportunity to make a showing that their contracts should be shortened or terminated. Based on our experience in the natural gas area, we have learned that it is critical to address these issues early, but we also have chosen an approach different from that taken in the gas area because of the different circumstances facing the electric industry.

In balancing the wide array of interests reflected in the rehearing petitions, we have made a number of clarifications and granted rehearing on some issues, but we reaffirm the core elements and framework of Order No. 888. Since the time the final rules issued, as discussed in Section III, the pace of competitive change has continued to escalate in the industry at both the wholesale and retail levels as competitors, customers and state regulatory authorities aggressively seek ways to lower the price of electricity. We therefore believe it is all the more critical that we remedy undue discrimination

in interstate transmission services now, and that we do so generically, if we are to fulfill our responsibilities under the FPA to protect consumers and provide a fair and orderly transition to new competitive markets.

Finally, with respect to environmental issues associated with this rulemaking, certain parties on rehearing continue to challenge the adequacy of our Final Environmental Impact Statement (FEIS). The central issues are whether the Final Rule will increase emissions of nitrogen oxides (NO_x) from certain fossil-fuel fired generators, which could affect air quality in downwind areas to which these emissions may be carried, and the Commission's authority to mitigate environmental consequences.

[30,178]

We deny rehearing on the environmental issues raised and affirm our conclusion that we have satisfied our obligations under NEPA. As discussed in detail in the Final Rule, this rulemaking is expected to slightly increase or slightly decrease total future NO_x emissions, depending on whether competitive conditions in the electric industry favor the utilization of natural gas or coal as a fuel for the generation of electricity. We also examined mitigation options over the longer term, and found that the preferred approach for mitigating any adverse environmental consequences would be for the Environmental Protection Agency (EPA) and the states to address the problem through regulatory authorities available under the Clean Air Act. The petitions for rehearing have not persuaded us to change this approach. Indeed, we note that since the issuance of Order No. 888, the EPA has concluded that the Rule is unlikely to have any immediate significant adverse environmental impact and thus concurred

that the Commission's analysis is adequate under NEPA. We further note that EPA has recently taken steps under the Clean Air Act to address NOx emissions as part of a comprehensive emissions control program, along the lines endorsed by the Commission in the EIS.

In summary, the Commission believes that our authorities under the FPA not only permit us to adapt to changing economic realities in the electric industry, but also require us to do so to eliminate undue discrimination and protect electricity customers. The measures required in Order No. 888 are necessary to remedy undue discrimination in interstate transmission services and provide an orderly and fair transition to competitive bulk power markets.

To assist the reader, we provide below a section-by-section summary of key elements of this Order on Rehearing.

Scope of the Rule

In this section we discuss petitions to rehear our requirement that transmission and power sales services be contracted for separately (unbundled). We reaffirm that this requirement is a reasonable and workable means of assuring non- discriminatory open access transmission. In doing so we refuse invitations to require that utilities under our jurisdiction divest themselves of generation or transmission assets. We do, however, make an important clarification involving how we will deal with existing contracts that contain so-called Mobile-Sierra clauses (clauses under which one or both parties agreed not to seek modification of contract terms unless they could show that it is contrary to the public interest not to permit the modification).

In Order No. 888 we concluded that contracts would not be abrogated by operation of the Rule. Instead, preexisting contracts would continue to be honored until such time as they were revised or terminated. We also found that those who were operating under pre-existing requirements contracts containing *Mobile-Sierra* clauses would nonetheless be allowed to seek reform of the contracts on a case-by-case basis. On rehearing we affirm that public utilities will be allowed to file to amend their *Mobile-Sierra* contracts for the limited purpose of providing an opportunity to seek recovery of stranded costs, without having to make a public interest showing that such cost recovery should be permitted. However, these utilities will have the burden, on a case-by-case basis, of showing that they had a reasonable expectation of continuing to serve the departing customer after the contract term. We clarify that if the utilities under such contracts seek to modify provisions that do not relate to stranded costs, they will have the burden of showing that the provisions are contrary to the public interest.

We here make clear that, in turn, customers will be allowed to file to amend their *Mobile-Sierra* contracts to modify any contract term or to terminate the contract, without having to make a showing that the contract terms are contrary to the public interest. Instead, customers seeking modifications must demonstrate that the provisions they wish modified are no longer "just and reasonable." We reaffirm our conclusion in the Final Rule that if a customer seeks to shorten or eliminate the term of its contract, however, any contract modification approved by the Commission will provide for appropriate stranded cost recovery by the customer's supplying utility.

These various provisions meet the two-fold need to deal with stranded costs and the contracts under which those costs were incurred. However, as described in **[30,179]** Order No. 888, the opportunity to reform Mobile-Sierra contracts extends only to a limited set of contracts -- those entered into on or before July 11, 1994, for requirements power.

Comparability

In this section we deal with those requesting rehearing of our conclusions regarding what "comparable" service is, who is eligible for that service, and how it is to be implemented. We reaffirm our finding that, as a matter of law, we have jurisdiction over the rates, terms and conditions of unbundled transmission service provided to retail customers. We also clarify that we have authority to order "indirect" unbundled retail transmission services and that if such transmission is ordered by us in the future, or if it is provided voluntarily, otherwise eligible customers may obtain such service under the open access tariff. We expect public utilities to provide such service in the future and, if they do not, we will not hesitate to order it.

We modify in two respects the definition of who is eligible for open access transmission service. First, we clarify that, with respect to service that this Commission is prohibited from ordering by section 212(h) of the Federal Power Act (retail wheeling directly to an ultimate consumer and "sham" wholesale wheeling), entities are eligible for such service under the tariff only if it is provided pursuant to a state requirement or is provided voluntarily. Second, we clarify that retail customers taking unbundled service pursuant to a state requirement (i.e., direct retail service) are eligible for

such service only from those transmission providers that the state orders to provide service. These changes are made to make clear that our rules cannot be used to circumvent the proscriptions placed on the Commission against ordering direct retail wheeling.

Ancillary Services

In this section we deal with petitions to rehear our definitions of ancillary services -- those services such as scheduling, voltage control, and supplemental reserve service that must or can attend the providing of transmission service -- as well as the provisions involving these services. We reaffirm that tariffs must separately state the charges for these services. We do modify some of the definitions of these services to conform to industry needs and practices. Most importantly, we make clear that the transmission provider's sale of ancillary services associated with providing basic transmission service is not a wholesale merchant function and thus does not violate the standards of conduct imposed with Order No. 889.

Coordination Arrangements

The requirement to provide non-discriminatory open access transmission applies to any agreement between utilities that contains transmission rates, terms or conditions. This includes pooling arrangements and agreements between companies contracting to provide each other mutually beneficial transmission services. In Order No. 888 we laid out rules under which the open access comparability requirements would apply to tight and loose power pools, public utility holding companies and bilateral coordination agreements. We

also set out principles that would govern our approval of independent system operator (ISO) agreements.

In this section we affirm the rules governing coordination agreements. In doing so we clarify the definition of "loose pool." We also make clear that, unlike in other situations where we require utilities to provide not only the services they provide themselves but those they could provide themselves, we will require members of loose pools to offer to third parties only those transmission services that they provide themselves under their pool-wide agreements.

We also reaffirm our strong commitment to the concept of ISOs and the ISO principles described in Order No. 888. In doing so we reject arguments that we should require that ISOs be formed. At the same time, we emphasize that while there is no "cookie-cutter" approach to forming an acceptable ISO, the requirement of fair and non-discriminatory rules of governance (Principle One) and the requirement that ISO employees have no financial interest in the economic interests of power marketers - - backed by strict conflict of interest provisions -- (Principle Two) are fundamental to our approving any ISO.

Pro Forma Tariff Provisions

The *pro forma* tariff is the basic mechanism implementing the requirements of comparable open access transmission. It **[30,180]** provides the details of the transmission service obligations imposed on jurisdictional utilities by the Rule. On rehearing we affirm most of the provisions set out in Order No. 888 for the *pro forma* tariff. We do make changes to conform the *pro forma* tariff to

changes adopted under other sections (for example, the definition of "eligible customer").

The rehearing petitions raised many questions about how particular aspects of the tariff will work. For the most part, these questions cannot be answered generically, but must be resolved on a case-by-case basis in the context of specific fact situations. However, the petitions brought to light issues that require clarifications and in some cases revisions to the tariff. The most significant of these involve discounting practices, provisions governing priority of service and curtailment, and the reciprocity provision.

Discounting practices. Originally, we provided different rules depending upon whether the transmission provider was offering a discount to itself or an affiliate or offering a discount to a non-affiliate. In response to the rehearing petitions, we are making three significant changes to the discounting requirements to better permit the ready identification of discriminatory discounting practices while also providing greater discount flexibility.

First, any discount offered on transmission services (including supporting ancillary services) by a transmission provider or requested by any customer must now be made only over the OASIS. With this change, all will have the same, timely access to discounted services. In making this change, we clarify that a transmission provider may limit its discounted service to particular time periods.

Second, once the provider and customer agree on a discount, the details of the discounted service -- the price,

points of receipt and delivery, and length of service -- must be immediately posted on the OASIS.

Third, we revise our Rule respecting what other transmission paths must be offered at a discount. Originally, in Order No. 888, we required that when a discount was offered over one path, the transmission provider would have to provide that discount over all other unconstrained paths on its system. We will no longer require this. Instead, the discount will be limited to those unconstrained paths that go to the same point(s) of delivery as the discounted service being provided on the transmission provider's system. The discount will extend for the same time period and must be offered to all transmission service customers.

Priority and Curtailment. We affirm the right of first refusal policy that reservation priority continues for firm service customers served under a contract of one year or more. We also affirm that curtailment must be made on a pro-rata basis and clarify that non-firm point-to-point service is subordinate to firm service. However, we clarify that the pro-rata curtailment requirement extends to only those transactions that alleviate the constraint.

Reciprocity. In Order No. 888 we conditioned the use of a public utility's open access service on the agreement that, in return, it is offered reciprocal service by non-public utilities that own or control transmission facilities. Such reciprocal service does not have to be through an open access tariff, i.e., a tariff available to all eligible customers, but may be limited to those public utilities from whom the non-public utility obtains open access service. We affirm the reciprocity

condition. In doing so, however, we make several clarifications.

First, a public utility is free to offer transmission service to a non-public utility without requiring reciprocal service in return. In other words, it may voluntarily waive the reciprocity condition. However, if it chooses to do so, transmission service must be provided through the pro forma tariff. Alternatively, bilateral agreements for transmission service provided by the public utility will not be permitted.

Second, we clarify that under the reciprocity condition a non-public utility must agree to offer the Transmission Provider any transmission service the non-public utility provides or is capable of providing on its system. This means that the non-public utility undertaking reciprocity must have an OASIS and must operate under the standards of conduct imposed under Order No. 889 unless it is granted a waiver by the Commission or, where appropriate, by a regional transmission group (RTG) of which it is a member. We also clarify that a non-public utility cannot avoid its responsibilities by **[30,181]** obtaining transmission service through other transmission customers. Further, the seller as well as the buyer in the chain of a transaction involving a non-public utility will have to comply with the reciprocity condition.

Third, we adhere to our decision not to treat generation and transmission (G&T) cooperatives and their member distribution cooperatives as a single unit. Thus, the reciprocity provision extends to the G&T Cooperative and not to its member distribution cooperatives.

Fourth, we clarify the "safe harbor" provision under which a non-public utility may get a Commission decision that its transmission tariff suffices to meet reciprocity. A non-public utility may limit the use of any reciprocity tariff that it voluntarily files at the Commission to those transmission providers from whom the non-public utility obtains open access service. A non-public utility also may satisfy reciprocity through bilateral agreements with a public utility. As a related matter, if a public utility believes a non-public utility is violating the reciprocity condition, it may file with the Commission a petition to terminate its service to the non-public utility.

Fifth, we clarify that non-public utilities may include stranded cost provisions in their reciprocity tariffs.

Sixth, the order on rehearing removes the term "interstate" from the reciprocity provisions. This is to make clear that reciprocity applies even to those who do not own or control interstate transmission facilities; *i.e.*, foreign utilities and those located in the ERCOT region of Texas.

As to local furnishing bonds held by some public utilities, we clarify that all costs associated with the loss of tax-exempt status of those bonds caused by providing open access transmission service are properly considered costs of providing that service. This includes costs of defeasing, redeeming, and refinancing those bonds.

Other Clarifications. In this order on rehearing we take the opportunity to clarify various other tariff provisions. Among these: Transmission providers do not have to take service under the open access tariff for transmitting power

purchased on behalf of their bundled retail customers. Also, the ability to reserve capacity to meet the reliability needs of a transmission provider's native load applies equally to present transmission and transmission that is built in the future.

Implementation

On rehearing, we make no substantive changes to the implementation provisions originally required under Order No. 888. For the most part, the implementation process has been completed. Utilities have made the requisite tariff and compliance filings and public and non-public utilities have, through other orders, been provided guidance as to obtaining waivers of Order No. 888 and Order No. 889 requirements.

We emphasize that we do not require the abrogation of existing contracts. Rather, the Rule requires only that transmission providers offer transmission under the open access tariff in addition to existing service obligations. Commitments made under existing contracts will continue. Of course, both transmission providers and their customers may seek to revise the terms and conditions of existing contracts by making the necessary filings, as appropriate, under Sections 205 or 206 of the Federal Power Act.

State and Federal Jurisdiction

On rehearing we reaffirm our decision that when transmission service is provided to serve retail customers apart from any contract for the retail sale of power, i.e., when it is provided on an unbundled basis, that transmission service is under our jurisdiction. In today's market, and increasingly

in the future as more states adopt retail wheeling programs, retail transactions are, and will be, broken down into products that are sold separately -- transmission and generation -- and sold by different entities. The exercise of our jurisdiction over the rates, terms and conditions of unbundled retail transmission will, therefore, become more important. We also recognize that states have jurisdiction over facilities used for local distribution.

On rehearing we also reaffirm the seven-factor test of Order No. 888 to distinguish transmission under our jurisdiction from state-jurisdictional local distribution. In doing so, we recognize that our test does not resolve all possible issues. There may be other factors that should be taken into account. The test, therefore, is designed for flexibility to include unique local characteristics and usages. To that end, we will continue to defer to state findings on these matters.

In addition, we clarify that states have the authority to determine the retail marketing areas of the electric utilities within their respective jurisdictions. We also recognize that states have the concomitant authority to determine the end user services these utilities provide.

Stranded Costs

On rehearing, we reaffirm our basic decisions surrounding the recovery of stranded costs. Utilities will be allowed the opportunity to seek to recover legitimate, prudent, and verifiable wholesale stranded costs. This opportunity is limited to costs associated with serving customers under wholesale requirements contracts executed on or before July

11, 1994 that do not contain explicit stranded cost provisions; and costs associated with serving retail-turned-wholesale customers.

We clarify that we will consider on a case-by-case basis whether to treat a contract extended or renegotiated without a stranded cost provision as an existing contract for stranded cost purposes.

In each case, the opportunity to seek stranded costs is limited to situations in which there is a direct nexus between the availability and use of a Commission-required transmission tariff and the stranding of the costs. The Rule does not allow the recovery of costs that do not arise from the new, accelerated availability of non-discriminatory transmission access.

The Commission also reaffirms its decision that stranded costs should be recovered from the customer that caused the costs to be incurred. The Commission is not requiring other remaining customers, or the utility, to shoulder a portion of its stranded costs that meet the requirements for recovery.

The Commission, as described in Order No. 888, will be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers. With respect to such cases, we have made several changes.

First, the Commission has reconsidered its decision respecting cases involving existing municipal utilities that annex retail customer service territories. Under Order No. 888, we found that in such cases the Commission should not

be the primary forum for determining stranded cost recovery. On rehearing we now find that such cases should fall within our province.

Second, we clarify that the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers applies regardless of whether the customer or its new supplier is the one requesting and contracting for the transmission service. To this end, we have revised the definition of "wholesale stranded cost."

With respect to the recovery of stranded costs caused by unbundled retail wheeling, we affirm that the only circumstance in which we will entertain requests for these types of costs is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required. We clarify that if a state regulatory authority has in fact addressed such costs, regardless of whether it has allowed full recovery, partial recovery or no recovery, utilities may not apply to the Commission to recover stranded costs caused by the retail wheeling.

Other

In this section we resolve questions concerning our information reporting requirements, regional transmission groups, and the special situations posed by utilities in the Pacific Northwest and by federal power marketing and similar agencies. Here we make some minor clarifications but make no significant changes to Order No. 888.

We are not persuaded that the information reporting requirements need to be changed at this time. Finally, we reject arguments that would have us fix generically any particular rate methodology for providing open access transmission service under the *pro forma* tariff.

* * * * *

[pp. 30,208 - 30,218]

[30,208]
The Commission's General Counsel Never Asserted, Or Even Suggested, That The Commission Does Not Have The Authority To Order Wheeling As A Remedy For Undue Discrimination

Union Electric spends several pages of its rehearing request asserting that the Commission's own General Counsel has acknowledged the limitations on the Commission's authority to order wheeling.[98] In particular, it points to a statement by a Commission OGC witness that "'if Congress intends for the Commission to be able to deal with transmission on its own motion and thereby go further than simply dealing with industry proposals,' Congress would need 'to include an affirmative statement somewhere in the Act that the Commission could require wheeling on its own motion.'"[99] This same statement was previously raised by EEI and previously addressed in Order No. 888. We do not

[98]Union Electric at pp. 37-40.

[99]Union Electric at pp. 38-39.

disagree that this statement was made. However, it must be read in the context of the witness' entire testimony in which the witness stated *four* times the view that the case law supports the argument that the Commission has authority to order wheeling as a remedy for undue discrimination.[100] Indeed, contrary to Union Electric's assertion, the extensive legal analysis set forth by the Commission's witness supports the position relied upon in this proceeding.[101] Thus, viewed in

[100]Hearings on H.R. 1301, H.R. 1543, and H.R. 2224 before the Subcommittee on Energy and Power of the House Committee on Energy and Commerce, 102d Cong., 1st Sess. (May 1,2 and June 26, 1991), Statement of Cynthia A. Marlette, Associate General Counsel, Federal Energy Regulatory Commission, Report No. 102-60 at p. 60 ("However, as discussed below, there are strong legal arguments that the Commission's obligation to protect against undue discrimination carries with it the authority to impose transmission requirements as a remedy for undue preference or discrimination." "As discussed below, although the case law in this area has been uncertain, in OGC's opinion there is a strong legal argument that the Commission can require transmission as a remedy for undue preference or undue discrimination."); at pp. 69-70 ("The weight of the limited case law, particularly the AGD opinion, supports authority to order wheeling as a remedy for undue discrimination where substantial evidence exists."); at p. 106 ("I believe that we have substantial authority under the existing case law to mandate access where necessary to remedy anticompetitive effects.").

[101]The statement quoted was preceded by a legal analysis of the Commission's authorities under then existing law, including section 206, and a statement that an examination of the Commission's full authorities might further open up the industry. Further, it was made in the context of case-by-case industry

the context of the witness' entire testimony, Union Electric's arguments to the contrary are unavailing. Moreover, nowhere did the witness ever suggest, as asserted by Union Electric, that FPA sections 205 and 206 could only be used "to eliminate unduly discriminatory terms in a wheeling arrangement voluntarily filed with the Commission."[102]

The Commission Has The Authority To Order Public Utilities To Make Rate Filings In This Proceeding

We reject Union Electric's argument that our requirement that Group 2 Public Utilities make section 205 filings is contrary to the voluntary filing scheme inherent in section 205. It is true that the Commission ordinarily cannot require a utility to make a section 205 filing. However, in this situation the section 205 filing was required as a remedy under section 206 of the FPA to establish rates for non-discriminatory open access transmission. Acting pursuant to section 206 of the FPA, we found that undue discrimination exists in the wholesale transmission of electric power and ordered the filing of non-discriminatory open access transmission tariffs to remedy this discrimination. Section 206 further requires that upon such a finding the Commission "shall determine the just and reasonable rate, charge, classification, rule, regulation, **[30,209]** practice, or contract to be thereafter observed and in force. . . ." Thus, we had the

---

proposals and the Commission's inability to require case-by-case wheeling on its own motion. It did not address section 206 authority to remedy undue discrimination.

[102]Union Electric at p. 39. We note that Union Electric did not cite to any page or particular language to support its assertion.

authority to set the rates that would be observed and in force following the effectiveness of open access transmission and initially proposed to set rates for each public utility. However, rather than take this intrusive approach, which necessarily would have required a number of generic assumptions and resulted in less than public utility-specific rates, upon issuance of the Final Rule, we chose to permit these public utilities to make section 205 filings to propose their own rates for the services provided in the *pro forma* tariff.

The Commission's Prior Failure To Order Wheeling As A Remedy For Undue Discrimination Is Not Dispositive

After discussing several cases that it asserts address the Commission's authority to remedy undue discrimination, Carolina P&L declares that "[p]erhaps the strongest evidence that the Commission lacks the power to compel wheeling under FPA section 206 is the fact that the Commission has never previously exercised this alleged power, despite numerous opportunities to do so."[103] However, the court in AGD succinctly dismissed a similar argument:

> It is finally argued that the Commission's not having imposed any requirements like those of Order No. 436 in the period from enactment in 1938 until the present demonstrates the lack of any power to do so. . . . But as our introductory review of the economic background sought to illustrate, the Commission here deals with conditions that are

---

[103]Carolina P&L at pp. 35-36.

> altogether new. Thus no inference may be drawn from prior non-use.[104]

Undue Discrimination/Anticompetitive Effects[105]

A number of utilities and state commissions argue that the Commission lacks evidence to support a finding of undue discrimination.[106]

VA Com argues that the Commission failed to make a legally supportable finding of industry-wide undue discrimination: "FERC apparently drew a conclusion that there was undue discrimination in the NOPR without support and later accepted customers' allegations, without further inquiry, and relied on them in making its finding of industry-wide undue discrimination." (VA Com at pp. 2-3).

PA Com and Carolina P&L assert that allegations of undue discrimination do not form a sufficient basis to compel a generic rulemaking. Not coming forward with specific

---

[104]824 F.2d at 1001. In this regard, we acknowledge that our view of what constitutes undue discrimination has evolved significantly in light of the dramatic economic changes in the industry, as described briefly above and more fully in Order No. 888.

[105]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,682-84; *mimeo* at pp. 136-42.

[106]*E.g.*, El Paso, Union Electric, Carolina P&L, VA Com, FL Com, PA Com.

accusations and the identity of specific accusers, PA Com asserts, is unconstitutional as a deprivation of due process.

With regard to specific allegations of undue discrimination, SoCal Edison argues that the Commission inappropriately relied upon allegations involving SoCal Edison as evidence of undue discrimination. SoCal Edison asks that the Commission declare that it is not making a factual determination as to any particular allegation especially since prior to 1994 the Commission defined discrimination differently. Dalton similarly argues that the Commission has no basis for finding that Georgia Power Company is engaged in unlawful undue discrimination as to new or roll-over transmission services in the operation of the Integrated Transmission System in Georgia (ITS) under the ITS agreement. Moreover, Dalton argues, even if it is found that GPC acted in unduly discriminatory manner, it is not practical or lawful to order open access tariff for new and roll-over services.

Finally, Carolina P&L argues that the comparability standard does not eliminate the "requirement" that parties must be similarly situated before discrimination is present, and that the Commission has not provided factual support for its implicit finding that public utilities and their native load customers are similarly **[30,210]** situated to third parties. It cites *City of Vernon v. FERC*, 845 F.2d 1042 at 1045-46 (D.C. Cir. 1988), in support.

Commission Conclusion

As an initial matter, the Commission grants SoCal Edison's request for clarification that in Order No. 888 we

did not make a factual determination as to any particular allegation of past discrimination described in the Final Rule.[107] However, we reject arguments that the Commission cannot rely in part on the array of allegations and circumstances raised by customers in individual cases over the years and brought forth in response to the NOPR. The specific allegations are illustrative. However, they present examples of the types of discriminatory incentives and behavior inherent in ownership of monopoly transmission facilities, and also present credible examples of the types of discriminatory behavior in which public utilities could engage in the future. We also reject arguments that customers and the Commission must litigate and make specific findings of discrimination against each public utility before we can take any action to preclude discriminatory behavior that will harm competition and, ultimately, electricity consumers. This is particularly true where the discriminatory behavior clearly is in the economic self-interest of a monopoly transmission owner facing the markedly increased competitive pressures that are driving today's electric utility industry. As we recognized in Order No. 888,

> [t]he inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by

---

[107]In response to PA Com's and Carolina P&L's assertions that not coming forward with specific accusations and identities of specific accusers is unconstitutional and a deprivation of due process, we emphasize that the Commission has not denied due process to anyone. The Final Rule does not, nor is it intended to, make specific findings as to any particular utility or any particular allegation raised.

> refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices. As the AGD court stated: "Agencies do not need to conduct experiments in order to rely on the prediction that an unsupported stone will fall."[108]

We believe that the same general discriminatory circumstances that faced us when we required open access transportation in the natural gas industry[109] are also before us today in the electric industry. First, it is uncontested that market power continues to exist in the ownership and operation of the monopoly-owned facilities that comprise the nation's interstate transmission grid. Second, utilities, as a general matter, did not in the past offer comparable transmission services to competitors or to customers. Open access services simply were not made available by utilities until the late 1980s when the Commission began to impose open access as a condition of approval of market-based rates and utility mergers in order to mitigate market power and remedy anticompetitive effects. Rather, the vast majority of utilities historically have declined to transport electric energy that would compete with their own sales or have offered access that is inferior to what they use for their own sales. Third, discrimination in transmission services, when viewed in light of utilities' own uses of their transmission systems

---

[108]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 331,682; *mimeo* at pp. 136-37.

[109]*See AGD*, 824 F.2d at 999-1000.

compared to what they offer third parties, has denied and will continue to deny customers access to electricity at the lowest reasonable rates. The entities on rehearing have raised nothing to persuade us that it is in the interests of consumers to maintain the self-evident incentives for transmission owners to exercise their monopoly power over transmission to discriminate in favor of their own generation sales -- incentives that will only increase in the future as competitive pressures continue to escalate.

The Commission addressed the same argument as that being made by Carolina P&L, that the Commission has not made the requisite finding that third-party transmission customers are similarly situated to public utilities and their native load customers, in 1994 in the *NEPOOL* **[30,211]** and *AEP* cases.[110] In these cases, we recognized that the traditional focus of our undue discrimination analysis had been whether factual differences justify different rates, terms and conditions for similarly situated customers, but concluded that due to changing conditions in the electric utility industry, it was necessary to reevaluate our traditional analysis. As we stated in *NEPOOL*, the focal point of undue discrimination claims has shifted from claims of undue discrimination in rates and services which the utility offers different customers to claims of undue discrimination in rates and services which the utility offers when compared to its own use of the transmission

---

[110]*New England Power Pool*, 67 FERC ¶61,402 (1994) (*NEPOOL*); *American Electric Power Service Corporation*, 64 FERC ¶61,279 (1993), *reh'g granted*, 67 FERC ¶61,168, *clarified*, 67 FERC¶61,317 (1994) (*AEP*).

system.[111] "In this context, framing the analysis in terms of how a public utility treats similarly situated customers is not applicable or instructive."[112] The Commission concluded that it therefore must reexamine its application of the standard for undue discrimination claims under sections 205 and 206 of the FPA. The Commission further elaborated on its re-examination of undue discrimination in AEP. The Commission cited its NEPOOL discussion and set for hearing the different uses that AEP made of its transmission system and whether there were any operational differences between any particular use that AEP made of the system and the use third parties might need, and, in particular, the degree of flexibility AEP accorded itself in using its transmission system for different purposes. The Commission subsequently set the same issue for hearing in several other cases.[113] In the NOPR, however, the Commission concluded that based on what it had learned in the ongoing cases, it would address this issue generically in this rulemaking. We announced in the NOPR our belief that all utilities use their own systems in two basic ways: to provide themselves point-to-point transmission service that supports coordination sales, and to provide themselves network transmission service that supports the economic dispatch of their own generation units and purchased power resources (integrating their resources to meet their internal load). Third parties may need one or both

---

[111]67 FERC ¶61,042 at p. 61,132.

[112]*Id.*

[113]*Commonwealth Edison Co.*, 70 FERC ¶61,204 (1995); *Wisconsin Electric Power Co.*, 70 FERC ¶61,074 (1995); and *Wisconsin Public Service Corp.*, 70 FERC ¶61,075 (1995).

of these basic uses in order to obtain competitively priced generation or to have the opportunity to be competitive sellers of power, and the Commission proposed that all public utilities must offer both services on a non-discriminatory open access basis.[114]

We affirmed this determination in the Final Rule. We concluded that a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others. Because a public utility that is reasonably capable of providing transmission services may provide itself such services at any time it finds those services desirable, it is irrelevant that it may not be using or providing that service today.[115] Thus, based on the analysis in this record, the Commission has determined that undue discrimination in the provision of transmission services in today's industry does not turn on whether utilities and their native load customers are similarly situated to third parties, but instead turns on whether the utility is providing comparable service, that is, service that it is reasonably capable of providing to other users of the interstate transmission system.

In short, the Commission is not bound to a static application of its undue discrimination analysis under the FPA and, indeed, has a public interest responsibility to reexamine undue discrimination in light of changed circumstances in the

---

[114]*FERC Statutes and Regulations* ¶32,524 at p. 33,079.

[115]*FERC Statutes and Regulations* at p. 31,690; *mimeo* at p. 160.

industry.[116] That is what we began in NEPOOL and AEP and have completed in this rulemaking. The traditional "similarly **[30,212]** situated" test, while applicable to discrimination among third-party customers, simply is not applicable when analyzing discrimination between third-party transmission customers and transmission owners. Under Carolina P&L's theory, presumably the only customers that could be shown to be similarly situated would be those who own monopoly transmission facilities and have native load (i.e., captive) customers. This would preserve customer captivity, perpetuate monopoly power and profits, and deny the lowest reasonable rates to consumers. We therefore reject Carolina P&L's arguments.

Moreover, the fact that public utilities and their native load customers have been treated differently from third-party transmission customers because they are not among those traditionally considered to be "similarly situated" is precisely the target at which Order No. 888 takes aim. Historically, competitively-priced power was not broadly available to wholesale customers because the industry was dominated by

---

[116]There is no "requirement" in the FPA that the Commission apply a "similarly situated" test. Carolina P&L's reliance on City of Vernon is misplaced. That case involved a claim of discrimination in the type of service offered to a wholesale customer versus that offered to retail customers, and the Commission's application of the "similarly situated" and "same service" test. Contrary to Carolina P&L's implication, the case does not hold that the Commission is bound to apply a "similarly situated" test in analyzing undue discrimination claims under the FPA.

vertically integrated IOUs[117] and, to the extent cheaper generation alternatives were available in the marketplace, transmission owners either took the cheaper power for their own uses or purchased and re-sold it at a profit.[118] Prior to EPAct, most power customers took power from the vertically integrated utilities that provided their transmission service. Transmission-only transactions played a secondary role in bulk power markets, facilitating certain economy transactions and coordination and pooling arrangements that improved utility operational efficiencies, largely as a complement to bundled bulk power transactions. Given the predominantly vertically-integrated industry and efficiencies that could be gained through encouragement of coordination and pooling transactions, the Commission was willing to accept utility practices that provided third parties with transmission services that were distinctly inferior to the utility's own uses of the transmission system.

In the future, however, unbundled transmission service will be the centerpiece of a freely traded commodity market in electricity, in which all wholesale customers can shop for power. In a market characterized by a significant increase in

---

[117]I.e., investor-owned utilities that owned generation, transmission and distribution facilities and most of whom had captive customers.

[118]Very simply, the transmission owner was able to prevent third parties from achieving the maximum savings possible in the generation market by withholding or delaying transmission service. Alternatively, the transmission owner could purchase the power and resell it to the third party at a rate that reflected a mark-up from the first power sale.

non-vertically integrated power suppliers and competitively priced power that is now meaningfully available, it is no longer in the interest of wholesale customers for the Commission to tolerate the types of practices that were previously accepted. We cannot allow what have become unduly discriminatory practices to erect barriers between customers and the rapidly emerging competitive electricity marketplace. Accordingly, a primary goal of Order No. 888 is to provide that in the future transmission providers and third-party transmission customers are "similarly situated" in the quality of transmission service available to them.

C. Comparability

1. Eligibility to Receive Non-discriminatory Open Access Transmission

In the Final Rule, the Commission modified the definition of "eligible customer" and, among other things, clarified that any entity engaged in wholesale purchases or sales of electric energy, not just those "generating" electric power, is eligible.[119] The Commission also clarified that entities that would violate section 212(h) of the FPA (prohibition on Commission-mandated wheeling directly to an ultimate consumer and sham wholesale transactions) are not eligible. Further, the Commission clarified that foreign entities that otherwise meet the eligibility criteria may obtain transmission services. The **[30,213]** Commission also provided for service to retail customers in circumstances that

---

[119]*FERC Statutes and Reuglations, Regulations Preambles January 1991-June 1996* at pp. 31,688-90; *mimeo* at pp. 154-58.

do not violate FPA section 212(h). Persons that would be eligible section 211 applicants also would be eligible under the open access tariff.

a. Unbundled Retail Transmission and "Sham Wholesale Transactions"

Rehearing Requests

Several entities assert that there is an inconsistency between tariff language and preamble language and argue that section 1.11 of the tariff should be made consistent with the preamble to ensure that, absent a state-approved program, retail wheeling is not available under the tariff, no matter which party requests service.[120] They maintain that the limitation in section 1.11 that the transmission provider only must provide retail transmission service voluntarily or under a state-approved program appears to apply only when a retail customer is the purchaser, not when the transmission purchaser is an electric utility. They suggest the following language to remedy the problem: "however, such entity is not eligible for transmission service that would be prohibited by Sections 212(h)(1) and/or 212(h)(2) of the Federal Power Act, unless such service is provided pursuant to a state retail access program or pursuant to a voluntary offer of unbundled retail transmission service by the Transmission Provider." (PSE&G at p. 22; Carolina P&L at pp. 8-9).

Detroit Edison argues that the Commission should modify the definition to exclude any reference to transmission

---

[120]*E.g.*, SoCal Edison, PSE&G, Carolina P&L.

service provided to retail customers so as to avoid confusion and possible forum shopping. At the least, Detroit Edison argues, the Commission should modify the language to state that transmission service is available to an ultimate consumer to the extent, and only to the extent, that the service is authorized by a lawful state retail access program or pursuant to a voluntary offer of unbundled retail transmission service by the transmission provider.

NYSEG asserts that the Commission did not apply the section 212(h) limitation to service to retail customers under the tariff. NYSEG requests that the Commission clarify that it will not require retail wheeling beyond the scope of state-mandated retail access programs or beyond the terms of a transmission provider's voluntary offer of retail wheeling service.

Oklahoma G&E asks the Commission to clarify that the term eligible customer differentiates between a customer eligible to receive transmission service and a customer whose transaction is a sham or would result in mandatory retail wheeling and would therefore be prohibited by section 212(h).

NYSEG further asserts that the right of first refusal provision would permit a retail customer receiving wheeling service to continue to take that service upon expiration of its contract, which could require the transmission provider, in violation of section 212(h), to continue retail wheeling beyond the scope of its voluntary offer of service or beyond the scope of a state-mandated retail access program.

SoCal Edison argues that the Commission cannot compel a utility to supply retail transmission service if the

utility challenges the authority of the state to require retail wheeling and section 1.11 should be revised to reflect this.

IL Com declares that it "does not recognize FERC's claim of jurisdiction over retail transmission service provided directly to a retail customer and disputes that unbundled retail wheeling directly to a retail customer is a service provided in interstate commerce." (IL Com at 35). Thus, "if FERC's proposed 'deference' to states is to be given any effect, states must be allowed to determine whether the retail transmission component of the retail wheeling program will be provided pursuant to the utility's existing filed wholesale tariff or whether the retail transmission will be provided pursuant to a 'separate retail transmission tariff' that is different from the wholesale tariff." (IL Com at 36). IL Com concludes that it is inappropriate (and illegal if FERC is overturned on its retail transmission jurisdiction assertion) to include retail customers taking final delivery of unbundled power for their own end uses under retail wheeling programs as eligible customers.

[30,214]

PA Com argues that it is relevant whether a customer is receiving retail or wholesale service and redefining transmission and local distribution service does not automatically convey jurisdiction to the Commission.

CCEM asks that the Commission clarify that a retail customer eligible to seek transmission service should be able to seek transmission service not only from the transmission provider, but from any other transmission provider. CCEM also asks that the Commission add the word "ultimate" before the word transmission provider in section 1.11 of the tariff.

EEI asks the Commission to "clarify that the transmission service provider should be allowed to supplement the terms and conditions of the *pro forma* tariff with additional provisions that specifically relate to the totality of the transmission service being provided, including the use of distribution facilities and any other transmission facilities not currently included in wholesale rates." (EEI at p. 24 (emphasis in original)).[121]

Union Electric argues that a literal reading of the eligibility definition could require retail wheeling by utilities in states other than those required to participate in a particular retail wheeling program.

Commission Conclusion

The Commission agrees with those entities that argue that section 1.11 of the pro forma tariff does not explicitly prohibit "sham wholesale transactions" that could currently be arranged under the tariff by a utility applying for service and designating the retail customer as a point of delivery. We therefore have modified section 1.11 to clarify that, with respect to service that we are prohibited from ordering by section 212(h) of the FPA (whether direct retail wheeling or "sham" wholesale wheeling), otherwise eligible entities may obtain such service under the tariff only if it is pursuant to a state requirement that such service be provided or pursuant to a voluntary offer of such service. We also have modified the language to clarify that eligibility for unbundled direct retail service required by a state applies only to service from

---

[121]See also *CSW Operating Companies*.

transmission providers that the state orders to provide the service. The modified language states:

> Eligible Customer: (i) Any electric utility (including the Transmission Provider and any power marketer), Federal power marketing agency, or any person generating electric energy for sale for resale is an eligible customer under the tariff. Electric energy sold or produced by such entity may be electric energy produced in the United States, Canada, or Mexico. However, with respect to transmission service that the Commission is prohibited from ordering by Section 212(h) of the Federal Power Act, such entity is eligible only if the service is provided pursuant to a state requirement that the Transmission Provider offer the unbundled transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider. (ii) Any retail customer taking unbundled transmission service pursuant to a state requirement that the Transmission Provider offer the transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider, is an eligible customer under the tariff.

Regarding SoCal Edison's argument, the Commission stated in the Final Rule:

> Moreover, we are mindful of the fact that we are precluded under section 212(h) from

> ordering or conditioning an order on a requirement to provide wheeling directly to an ultimate consumer or sham wholesale wheeling. We therefore clarify that our decision to eliminate the wholesale customer eligibility requirement does not constitute a requirement that a utility provide retail transmission service. Rather, we make clear that if a utility chooses, or a state lawfully requires, unbundled retail transmission service, such service should occur under this tariff unless we specifically approve other terms.[122]

Therefore, the Commission is not compelling a utility to provide unbundled retail transmission service.[123] Rather, the Commission **[30,215]** requires that should such service be provided, either pursuant to state mandate or voluntarily, it must be provided pursuant to the pro forma tariff unless the Commission approves alternative terms and conditions.

---

[122]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,689-90; *mimeo* at p. 158.

[123]We also disagree with NYSEG's assertion that the right of first refusal provision would permit a retail customer receiving wheeling service to continue to receive service after the expiration of its contract and could require the transmission provider to continue wheeling beyond the scope of its voluntary offer of service or beyond the scope of a state-mandated retail access program. Section 212(h) of the FPA would override any provision, including the right of first refusal provision, that may be included in the pro forma tariff.

However, in light of CCEM's request that we clarify that a retail customer eligible to seek transmission service under the tariff should be able to seek service not only from the transmission provider, but also from any other transmission provider, and in light of Union Electric's concerns regarding retail service eligibility, we believe certain clarifications of our jurisdiction and of the statements made in Order No. 888 are necessary. The statements cited above that were made in Order No. 888 and the eligible customer tariff definition in (ii) above refer to direct retail transmission, i.e., the transmission of electric energy "directly" to an ultimate consumer. The Commission is prohibited by section 212(h)(1) of the FPA from ordering this type of retail transmission and that is why customers are eligible for such transmission under the tariff only if the transmission is pursuant to a state order or is provided voluntarily. However, on its face, section 212(h) does not prohibit the Commission from ordering public utilities to provide "indirect" unbundled retail transmission in interstate commerce, i.e., the transmission necessary to transmit unbundled electric energy to a utility that ultimately will deliver the energy to a customer that is purchasing the unbundled energy at retail either pursuant to a state retail access order or pursuant to voluntary delivery by the local utility.

We clarify that we believe we have the jurisdiction under the FPA to order indirect retail transmission to an ultimate consumer and that if the Commission under sections 205, 206 or 211 of the FPA orders such transmission, entities that otherwise qualify as eligible customers under the tariff will take transmission service for such indirect retail wheeling pursuant to the *pro forma* tariff. We note that the Commission may order such transmission on a case-by-case basis or may

determine to do so generically in the future. We expect public utilities to provide such indirect retail access under the *pro forma* tariff and, if they do not, we will not hesitate to order them to do so.

In response to IL Com's argument that it does not recognize this Commission's claim of jurisdiction over the rates, terms and conditions of unbundled retail transmission that is provided directly to an ultimate consumer, the Commission reaffirms its legal conclusion set forth in the Final Rule.[124] As to its claim that we should give deference to the state as to whether such service could be taken under the wholesale tariff or a separate retail tariff on file with the Commission, we reaffirm our conclusion to address this on a case-by-case basis. Since the Final Rule issued, the Commission has addressed this in several orders. In New England Power Company, the Commission stated:[125]

> As we explained in the Open Access Rule and in the New Hampshire Interim Order, we generally expect retail transmission customers to take service under the same Commission tariff that applies to wholesale customers.

---

[124]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,780 and appendix G (at pp. 31,966-81); *mimeo* at p. 428 and appendix G.

[125]75 FERC ¶61,356 at p. 62,141, *order on reh'g*, 77 FERC ¶61,135 (1996). In the order on rehearing, the Commission permitted a separate retail tariff to remain in effect for the duration of the retail electric pilot programs established in Massachusetts by Massachusetts Electric Company.

> While we generally will defer to state requests for a separate retail tariff to accommodate the design and special needs of a state retail access program, the Massachusetts Commission has made no such request in this case.[15]

---

[15] See Open Access Rule, *FERC Statutes and Regulations*, at p. 31,784; *New Hampshire Interim Order*, 75 FERC at p. 61,687 & n.3 (both noting that such a separate retail tariff must **[30,216]** be consistent with the Commission's open access policies and comparability principles). . . .

Subsequently, in New England Power Company, 76 FERC ¶61,008 (1996), the Commission granted a limited waiver of the Open Access Rule requirements for the New Hampshire retail electric competition pilot project. Specifically, the Commission waived the requirement for individual service agreements, and the requirement for customer deposits. The Commission further announced that:

> other public utilities that provide unbundled retail service under a *pro forma* tariff do not need to apply to retail customers the tariff provisions regarding individual service agreements or customer deposits, unless a state retail program so requires.[126]

Concerning EEI's request for clarification, the Commission stated in the Final Rule:

---

[126] 76 FERC at p. 61,024.

> all tariffs need not be "cookie-cutter" copies of the Final Rule tariff. Thus, under our new procedure, ultimately a tariff may go beyond the minimum elements in the Final Rule pro forma tariff or may account for regional, local, or system-specific factors. The tariffs that go into effect 60 days after publication of this Rule in the Federal Register will be identical to the Final Rule pro forma tariff; however, public utilities then will be free to file under section 205 to revise the tariffs, and customers will be free to pursue changes under section 206.[127]

Utilities are free to include customer-specific terms and conditions or terms and conditions limited to certain customers (*e.g.*, a distribution charge) in the customer's service agreement and/or the network customer's network operating agreement.

b. Transmission Providers Taking Service Under Their Tariff

Rehearing Requests

TAPS states that section 1.11 does not seem to require a transmission provider to take service for its purchases, but the preamble does (citing mimeo at 57, 191, 266 and

---

[127] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,770 n. 514; *mimeo* at p. 399 n. 514.

regulatory text in section 35.28(c)(2)). It argues that transmission providers should be required to treat their own usage of the transmission system to serve retail customers under the network service provisions of the tariff. TAPS argues that this result could be achieved through an ISO or by requiring transmission providers to abide by all non-price terms of Parts I and III of the tariff. TAPS also argues that the rates charged network customers must be developed on the same basis as the transmission component of retail rates. It states that the transmission provider's purchases would then be made under Part III of the tariff to the extent they are made for serving retail customers. It further asserts that the Commission's authority and obligation to consider transmission owners' service to retail load in establishing wholesale transmission rates has been long established. At the least, TAPS argues that the Commission should require that a transmission provider take its wholesale purchases under some tariff.

Similarly, Coalition for Economic Competition asks the Commission to clarify that the requirement to use the *pro forma* tariff for wholesale purchases and to functionally unbundle wholesale purchases and sales does not apply to purchases made solely to serve retail customers on a bundled basis. It asserts that there is conflicting language in Order No. 888 (citing *mimeo* at p. 191) and Order No. 889 (citing *mimeo* at p. 12) and the *pro forma* tariff. Coalition for Economic Competition asserts that the Commission does not have jurisdiction over transmission that is part of a bundled retail sale.

Commission Conclusion

Several parties have noted on rehearing that there is conflicting language among the Final Rule, Order No. 889 and the *pro forma* tariff as to whether and to what extent the transmission provider must take service for "wholesale purchases" under its own tariff. As discussed below, we clarify that a transmission provider does not have to "take service" under its own tariff for the transmission of power **[30,217]** that is purchased on behalf of bundled retail customers.

In a situation in which a transmission provider purchases power on behalf of its retail native load customers, the Commission does not have jurisdiction over the transmission of the purchased power to the bundled retail customers insofar as the transmission takes place over such transmission provider's facilities,[128] and therefore the pro forma tariff does not have to be used for such transmission. Moreover, we recognize that purchases made collectively on behalf of native load[129] cannot necessarily be identified as

---

[128]To the extent the transmission takes place on the interstate facilities of other public utilities, we would have jurisdiction over such transmission.

[129]Native load means "[t]he wholesale and retail power customers of the Transmission Provider on whose behalf the Transmission Provider, by statute, franchise, regulatory requirement, or contract, has undertaken an obligation to construct and operate the Transmission Provider's system to meet the reliable electric needs of such customers." Section 1.19 of the *pro forma* tariff.

going to any particular customer. However, the Commission does have jurisdiction over transmission service associated with sales to any person for resale, and such transmission must be taken under the transmission provider's pro forma tariff.[130]

Order No. 888, relying on the principle of comparability, established the terms and conditions for network service provided to network customers under the *pro forma* tariff. Network customers may include the transmission provider itself as well as any other entity receiving Network Integration Service. If the transmission provider purchases energy from another power supplier in order to make sales to its wholesale native load customers, it must take the transmission service necessary to transmit the power from its point(s) of receipt to its point(s) of delivery under the same terms and conditions as other Network Customers.[131] As we explained in *AES Power, Inc.*, network customers are entitled to make economy energy purchases from non-designated network resources at no additional charge on a basis

---

[130]All transmission in interstate commerce by a public utility in conjunction with a sale for resale of electric energy is jurisdictional and must be taken under a FERC-jurisdictional tariff. The same is true for all unbundled transmission in interstate commerce to wholesale customers, as well as to unbundled retail customers.

[131]Under the Order No. 888 pro forma tariff, third-party wholesale customers have the ability to obtain the identical service the transmission provider provides itself when it engages in a sale of electric energy for resale. This may include network or point-to-point service.

comparable to the economy energy purchases made by the transmission provider on behalf of its bundled retail customer.[132] This applies to the transmission provider as a network transmission customer under its own tariff as well as to other network transmission customers that make economy energy purchases on behalf of their customers. Thus, insofar as all wholesale transmission customer usage is concerned, third-party network customers are treated the same as the transmission owner.

2. Service that Must be Provided by Transmission Provider

In the Final Rule, the Commission found that a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others.[133] The Commission explained that because a public utility that is reasonably capable of providing transmission services may provide itself such services at any time it finds those services desirable, it is irrelevant that it may not be using or providing that service today. However, the Commission explained that if a customer seeks a customized service not offered in an open access tariff, a customer may, barring successful negotiation for such service, file a section 211 application.

---

[132]69 FERC ¶61,145 at p. 62,300 (1994) (proposed order), 74 FERC ¶61,220 (1996) (final order).

[133]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,690; *mimeo* at p. 160.

Rehearing Requests

Cleveland requests that the Commission make explicit that comparability will be evaluated not only by reference to a transmission provider's wholesale services, but also by comparison to the terms, conditions, and prices applicable to **[30,218]** its retail services, whether bundled or unbundled. Cleveland asserts that this is needed so that TDUs are not at a competitive disadvantage in competing with the transmission provider for retail customers. It maintains that this is consistent with the Transmission Pricing Policy and established precedent.

Commission Conclusion

No clarification is necessary. In determining what transmission services a utility must offer for wholesale sales of electric energy in interstate commerce, the Final Rule explicitly states that "a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others."[134] Further, the Final Rule requires that network service customers receive service comparable to the service provided to the transmission provider's native load. Because the Rule applies to retail transmission that is voluntarily offered or pursuant to a state retail access program, the requirements to offer services that the utility is reasonably capable of providing and services comparable to those

[134]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996 at p. 31,690; mimeo at p. 160.*

provided to native load would also apply to retail service in these limited retail circumstances.

* * * * *

[pp. 30,278 - 30,279]

[30,278]

3. Curtailment and Interruption Provisions[297]

a. Pro-Rata Curtailment Provisions

In the Final Rule, the Commission found that curtailment on a pro-rata basis is appropriate for curtailing transactions that substantially relieve a constraint.[298] The Commission explicitly allowed the transmission provider discretion to curtail the services, whether firm or non-firm, that substantially relieve the constraint.

[297]In the Final Rule *pro forma* tariff, the Commission defines curtailment as: "A reduction in firm or non-firm transmission service in response to a transmission capacity shortage as a result of system reliability conditions." (pro forma tariff section 1.7). The *pro forma* tariff defines interruption as: "A reduction in non-firm service due to economic reasons pursuant to Section 14.7." (*pro forma* tariff section 1.15). The distinction between curtailment and interruption may have been blurred in Order No. 888 and this order attempts to clarify that distinction.

[298]*FERC Statutes and Regulations, Regulation Preambles January 1991-June 1996* at p. at 31,749; *mimeo* at pp. 335-36.

The Commission also indicated that it would consider granting deference to an alternative curtailment method to avoid hydro spill if such a regional practice is generally accepted and adhered to across the region.

The Commission further found that under network and point- to-point service, the transmission provider may propose a rate treatment (penalty provision) to apply in the event a customer fails to curtail service as required under the Final Rule pro forma tariff and indicated that such proposals will be evaluated on a case-by-case basis on compliance.

Rehearing Requests

PA Com asserts that pro rata curtailment fails to hold native load harmless to the extent practical as required by the FPA. PA Com points out that on January 19, 1994, PJM initiated pro-rata load shedding, in part to preserve economic transactions, leaving customers in Pennsylvania without power during a record cold spell.

VA Com argues that pro rata curtailment may harm native load customers and section 206 complaints are after the fact and of little assistance to native load. VA Com argues that curtailment priority (in order of curtailment) should be: non-firm, contract firm, and then native load, and that utilities should have flexibility to curtail on a pro-rata basis within classes, subject to state curtailment policy.

Several entities argue that provision must be made for preference in curtailment priorities obtained through settlement, through payment of good and valuable

consideration, or under existing transmission contracts.[299] Turlock argues that customers should be able to obtain a variation from the pro rata scheme if they can show that they have made either past or future investments to improve constrained facilities and that the quid pro quo for their investment is improved curtailment priority.

Allegheny asks the Commission to clarify that it did not intend to require public utilities to shed (through pro rata curtailment) native transmission load customers in order to preserve some portion of service to through system users of the grid. According to Allegheny, the FPA mandates that service reliability to franchise customers must be maintained and through-system users are not similarly situated to native transmission load customers and should not be treated the same in an emergency because through system customers can protect themselves, but native transmission load customers cannot. Allegheny adds that failure to maintain system reliability would violate section 211 of the FPA.

CCEM asserts that hard and fast priority rules are needed to prevent inconsistent rules from developing for different utilities, pools, or control areas.

Commission Conclusion

Assertions that the pro-rata curtailment provision in the tariff may harm native load customers are misplaced. The Commission clarified in the Final Rule that it was not requiring a pro-rata curtailment of all transactions at the time

---

[299] *E.g.*, Santa Clara, Redding, TANC.

of a constraint, but rather curtailment of **[30,279]** those transactions, whether firm or non-firm, that effectively relieve the constraint.[300] The Commission also required that such curtailments be made on a non-discriminatory basis, including the transmission provider's own wholesale use of the system. The Commission further explained that the pro-rata curtailment provision was intended to apply to situations where multiple transactions could be curtailed to relieve a constraint. Of course, if curtailment of multiple transactions is necessary, non-firm service would be curtailed prior to firm service. However, the Commission established that, in emergencies, the transmission provider had the discretion to interrupt firm service under the tariff to ensure the reliability of its transmission system.

In terms of reliability, we believe that sufficient safeguards have been established to protect native load. In particular, the transmission provider is responsible for planning and maintaining sufficient transmission capacity to safely and reliably serve its native load. Order Nos. 888 and 889 permit the transmission provider to reserve, in its calculation of ATC, sufficient capacity to serve native load.

Allegations that a utility did not curtail on a non-discriminatory basis, but instead favored a certain class of customer or type of transaction should be filed in a section 206 complaint proceeding to be reviewed on a case-specific basis. While it is true that such complaints will be processed

---

[300] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,749; *mimeo* at p. 335.

on an after-the-fact basis, it is only on a fact-specific basis that such complaints can be fully and adequately reviewed.

Additionally, tariff section 14.7 does in fact establish that for curtailment purposes, non-firm point-to-point transmission shall be subordinate to firm transmission service and non-firm service may also be interrupted for economic reasons. However, adopting curtailment schemes based solely on classes of service, as proposed by the VA Com, is inappropriate. Specifically, VA Com's proposal to curtail all non-firm transmission transactions prior to firm transactions could exacerbate an emergency situation. For example, a curtailment could be necessary due to a constraint affecting northbound transactions. However, curtailing all non-firm transactions, including southbound transactions (or counterflows), could worsen the situation. Accordingly, the Commission believes the approach established in the Final Rule of allowing non-discriminatory curtailments of the transaction(s) that effectively relieve(s) the constraint is appropriate.

In response to CCEM's concerns regarding the potential for inconsistent rules for different utilities, pools or control areas, the Commission explained in the Final Rule that any proposed deviations from the non-price terms and conditions of the pro forma tariff, such as regional practices, must be adequately supported by the utility proposing the change.

Finally, Order No. 888 did not abrogate existing contracts;[301] therefore, customers with unique curtailment priorities established by pre-existing contracts would not have these priorities eliminated for the term of the existing contract.

* * * * *

[pp. 30,334 - 30,350]

[30,334]

I. Federal and State Jurisdiction: Transmission/Local Distribution

In the Final Rule, the Commission explained that after reviewing the extensive analysis of the FPA, legislative history, and case law contained in both the initial Stranded Cost NOPR and in the Open Access NOPR, and the comments received on that analysis, it reaffirmed its **[30,335]** assertion of jurisdiction over the transmission component of an unbundled interstate retail wheeling transaction.[451] The Commission also reaffirmed and clarified its determinations regarding the tests to be used to determine what constitute Commission-jurisdictional transmission facilities and what constitute state-jurisdictional local distribution facilities in

---

[301]We note that in Order No. 888 we partially modified existing economy energy coordination agreements. *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,666; *mimeo* at p. 91.

[451]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,780-85; *mimeo* at pp. 427-42.

situations involving unbundled wholesale wheeling and unbundled retail wheeling.

The Commission also explained that where states unbundle retail sales, it will give deference to their determinations as to which facilities are transmission and which are local distribution, provided that the states, in making such determinations, apply the seven criteria discussed in the NOPR and reaffirmed by the Commission. In addition, the Commission clarified that there is an element of local distribution service in any unbundled retail transaction, and further clarified other aspects of its jurisdictional ruling to preserve state jurisdiction over matters that are of local concern and will remain subject to state jurisdiction if retail unbundling occurs.

The Commission reaffirmed its legal determination that if unbundled retail transmission in interstate commerce occurs voluntarily by a public utility or as a result of a state retail access program, this Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission. The Commission found compelling the fact that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.

The Commission further explained that when a retail transaction is broken into two or more products that are sold separately, the jurisdictional lines change. In this situation, the Commission emphasized that the state clearly retains jurisdiction over the sale of the power, but the unbundled transmission service involves only the provision of

"transmission in interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission.

The Commission recognized that in asserting jurisdiction over unbundled retail transmission in interstate commerce by public utilities, it was in no way asserting jurisdiction to order retail transmission directly to an ultimate consumer. It explained that its assertion of jurisdiction is that if unbundled retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

The Commission further clarified that nothing in its jurisdictional determination changes historical state franchise areas or interferes with state laws governing retail marketing areas of electric utilities. It explained that while its jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over transmission in interstate commerce by public utilities.

The Commission also adopted a new section 35.27(b) as follows:

> Nothing in this part (i) shall be construed as preempting or affecting any jurisdiction a state commission or other state authority may have under applicable state and federal law, or (ii)

> limits the authority of a state commission in accordance with state and federal law to establish (a) competitive procedures for the acquisition of electric energy, including demand-side management, purchased at wholesale, or (b) non- discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

With respect to the Commission's adoption of the Open Access NOPR's functional/technical tests for determining what facilities are Commission-jurisdictional facilities used for transmission in interstate commerce and what facilities **[31,336]** are state-jurisdictional local distribution facilities, the Commission concluded that it could not divine a bright line for unbundled retail transmission by the public utility that previously provided bundled retail service to the end user. The Commission added that the limited case law, including *Connecticut Light & Power Company v. FPC (CL&P)* and *Federal Power Commission v. Southern California Edison Company* (the *Colton* case),[452] supports a case-by-case determination.[453] Accordingly, the

---

[452]324 U.S. 515 (1945) (*CL&P*); 376 U.S. 205 (1964) (*Colton*).

[453]The Commission included a detailed legal analysis in Appendix G to Order No. 888. The Commission explained that it was particularly persuaded by the Supreme Court's statement that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. *See CL&P*, 324 U.S. at 534-35).

Commission stated that its technical test, with its seven indicators, will permit reasoned factual determinations in individual cases.

The Commission made two clarifications regarding local distribution in the context of retail wheeling. First, it explained that even if its technical test for local distribution facilities were to identify no local distribution facilities for a specific transaction, states have authority over the service of delivering electric energy to end users. Second, the Commission explained that through their jurisdiction over retail delivery services, states have authority not only to assess retail stranded costs but also to assess charges for so-called stranded benefits, such as low-income assistance and demand-side management.

Thus, under this interpretation of state/federal jurisdiction, the Commission explained, customers have no incentive to structure a purchase so as to avoid using identifiable local distribution facilities in order to bypass state jurisdiction and thus avoid being assessed charges for stranded costs and benefits.

The Commission further determined that it is appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs.

In instances of unbundled retail wheeling that occurs as a result of a state retail access program, the Commission indicated that it will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for

local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[454] Moreover, the Commission indicated that it will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

As a means of facilitating jurisdictional line-drawing, the Commission stated that it will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, the Commission explained that, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the principles established in the Final Rule, the Commission indicated that it will defer to such classifications and/or cost allocations.

Furthermore, the Commission stated that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances. The Commission

---

[454]In order to give such deference, the Commission noted its expectation that state regulators will specifically evaluate the seven indicators and any other relevant facts and make recommendations consistent with the essential elements of the Rule.

explained that when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes -- a transmission component and a local distribution component. It again emphasized that the Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component. Thus, the Commission stated, **[30,337]** the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. However, the Commission added, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a separate retail transmission tariff[455] to accommodate the design and special needs of such programs. In such situations, the Commission indicated that it will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by the Final Rule. In addition, the Commission indicated that the rates must be consistent with its Transmission Pricing Policy Statement, and the guidance set forth in Order No. 888 concerning ancillary services.[456]

---

[455]The Commission noted that such a tariff could be different from the tariff that applies to wholesale customers, but that such tariff would still be filed with the Commission under FPA section 205.

[456]In applying the principles of the Final Rule to retail transmission tariffs, the Commission emphasized that it clearly cannot order retail wheeling directly to an ultimate consumer. (citing FPA section 212(h)).

The Commission also expressed concern, just as it did with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, the Commission reaffirmed its conclusion that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. Moreover, the Commission indicated that it will address these transactions on a case-by-case basis.

Rehearing Requests

Oppose Commission Assertion of Jurisdiction Over Unbundled Retail Transmission

Several state commissions indicate that, recognizing that the case law is not dispositive concerning the question of unbundled retail transmission services (either because the cases do not involve the transmission of power to retail customers or "fence off" local distribution from federal regulation), at least one court (*Wisconsin-Michigan Power Company v. FPC*, 197 F.2d 472 (7th Cir. 1952), *cert. denied*, 345 U.S. 934 (1953)) explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services.[457] Thus, they argue, the Commission should apply the wholesale versus retail analysis to the question of unbundled retail transmission.

---

[457]*E.g.*, NARUC, WI Com, WY Com.

IL Com asserts that retail transmission by a public utility directly to an end user has always (even before the FPA was enacted) been subject to regulation by the states. It contends that no change in law has occurred which justifies the Commission's claim of expanded jurisdiction. Moreover, it disagrees with the Commission's conclusion that the unbundled delivery by the previous public utility generation supplier directly to an end user is in interstate commerce. It argues that the FPA was never intended to disturb the jurisdiction of state regulators that existed prior to its passage and that retail transmission of electric energy by a public utility to an end user was under state jurisdiction before the Attleboro decision and has remained under state jurisdiction in the over sixty years following Attleboro. Even after unbundling, according to IL Com, transmission to a retail customer still involves a retail sale of transmission.

NARUC and VA Com assert that the legislative history provides little support for the Commission's conclusion that the act of unbundling generation from delivery serves to shift jurisdiction from a state commission to the Commission. If anything, they contend, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services. They assert that the Commission should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer are subject to the jurisdiction of the state commission regulating the utility, regardless of the identity of the party generating **[31,338]** or reselling the power or the facilities used to transport the power.

NARUC asserts that the Commission did not address a point raised in NARUC's reply comments as to how the removal of generation serves to unbundle the retail delivery function into separate transmission and distribution services. It maintains that the Commission simply assumes that a resulting transmission transaction is created when power is sold to a retail consumer by someone other than the utility delivering the power.[458]

MI & NH Coms ask the Commission to vacate those portions of the Rule that find that the Commission has jurisdiction over the transmission component of an unbundled retail sale in a local retail wheeling transaction. They assert that the Commission should confine its activity to wholesale transactions or those interstate transactions that do not implicate matters of local concern. They argue that the dual federal/state regulatory scheme establishes that Congress' intent is that state regulation of retail wheeling is not preempted by federal law as established in FPA section 201. They oppose unnecessary federal intrusion into local matters under a one-size-fits-all approach and assert that the retail wheeling initiatives in New Hampshire and Michigan are tailored to the unique utility environment in each state.

Central Illinois Light argues that unbundling of retail electric service does not change the states' longstanding jurisdiction over retail electric service and local distribution,

---

[458] *See also* IA Com (use of a utility's transmission system to serve its own retail customers is a bundled part of the retail sale transaction, which supports a simpler jurisdictional test holding that a movement of power by the last utility in any chain of delivery to a retail customer is a distribution transaction).

even when that service involves the use of transmission in interstate commerce. It asserts that 201(b)(1) ("transmission of electric energy in interstate commerce") cannot be read in a vacuum.

MN DPS & MN Com and OH Com assert that the Commission should have no role in the regulation of retail services, be they bundled or unbundled. They argue that, in refusing to grant the Commission authority over retail wheeling, Congress left jurisdiction over retail electric service to the states. They conclude that the Final Rule contains insufficient legal and/or policy justification for the Commission's assertion of jurisdiction over unbundled retail transmission services.

MN DPS & MN Com assert: "FERC bases its usurpation of state authority over retail transmission rates on its claim that balkanization would occur without the assertion of FERC authority. Therefore, the parties are entitled to rehearing so that this essential issue can be further analyzed." (MN DPS & MN Com at pp. 1-3).

FL Com argues that the Commission has not justified why the act of unbundling prices expands the Commission's jurisdiction into retail marketing areas. It argues that Section 212(g) of the FPA has the effect of prohibiting the Commission from usurping existing state jurisdiction over retail transmission service, whether bundled or unbundled. According to FL Com, FERC's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. It supports wheeling in jurisdiction for state commissions and wheeling out and wheeling through jurisdiction for the Commission.

IN Com opposes federalization of retail wheeling transactions within a state's boundaries as contrary to the FPA's legislative history and case law.

NJ BPU asserts that by claiming jurisdiction over unbundled retail transmission, the Commission is creating a disincentive for states to implement retail access because, by ordering retail access, the states may be relinquishing their jurisdiction over unbundled retail transmission terms and conditions -- jurisdiction that they would maintain under a bundled scenario.[459] PA Com argues that the Commission does not have the authority to order retail wheeling and that the jurisdictional formula is challengeable on engineering and legal grounds. It concludes that the Commission does not have jurisdiction over unbundled interstate retail transmission service. PA Com notes that the 1996 House and Senate hearings have **[30,339]** raised the question whether the Commission has the statutory authority to restructure the electric industry. PA Com questions the Commission's definition of the "traditional tasks of state and federal regulators" on the basis of section 201(b) of the FPA, the Supremacy Clause, and the Tenth Amendment of the U.S. Constitution.

Support Broader Assertion of Jurisdiction by the Commission Over Retail Wheeling

NY Utilities declare that the Commission has jurisdiction over retail wheeling from the source to the load, but does not have jurisdiction over transmission in bundled

---

[459] *See also* PA Com.

retail service. They assert that the Commission's reliance on state jurisdictional local distribution as a predicate to abstain from allowing retail wheeling stranded cost recovery is without foundation. They further assert that a unique element that sets local distribution apart from transmission is not the size of the facility or the length of travel, but that transportation is bundled with a retail sale. According to NY Utilities, the plain meaning of the FPA shows that local distribution is bundled retail service. They claim that the legislative history, to the extent necessary, and court cases support FERC jurisdiction over all aspects of retail wheeling, but makes clear that the Commission cannot regulate bundled retail service. They add that the NGA also demonstrates that local distribution means bundled retail service.

Commission Conclusion

In concluding that this Commission has exclusive jurisdiction over the rates, terms and conditions of unbundled retail transmission by public utilities in interstate commerce, the Commission in Order No. 888 thoroughly examined the statutory language of the FPA and its legislative history, and relevant FPA and NGA case law. While the state commissions on rehearing would like us to draw a bright line that gives them, to varying degrees, jurisdiction over retail interstate transmission by public utilities, no party on rehearing has raised any legislative history or case law that was not previously considered and that would support the proposition that states have jurisdiction over any unbundled transmission in interstate commerce. As explained below, we reaffirm our jurisdictional interpretation on rehearing and believe that it is

supported by the recent decision in *United Distribution Companies v. FERC.*[460]

Many of the rehearing arguments focus on the fact that states historically (even prior to the FPA) regulated retail transmission insofar as it was a component of bundled electric service to an end user, and they argue that by asserting jurisdiction over unbundled retail transmission, the Commission is somehow "taking away" jurisdiction the states previously had. The flaw in these arguments is their inherent assumption that jurisdiction over transmission service turns upon the question of whether the transmission service is being provided for "wholesale" or "retail" power sales. That is not the case. The question of jurisdiction rather turns upon the extent of the Commission's exclusive jurisdiction over transmission in interstate commerce under the FPA. The fact that states historically regulated most retail transmission service as a part of a bundled retail power sale is not the result of a legal requirement; it is the practical result of the way electricity has historically been bought and sold. However, the shape of power sales transactions is rapidly changing. Rather than claiming "new" jurisdiction, the Commission is applying the same statutory framework to a business environment in which, as discussed below, retail sales and transmission service are provided in separate transactions.

In the past, retails ales occurred almost exclusively on a bundled basis (i.e., the same entity provided a delivered

---

[460]88 F.3d 1105, 1152-53 (1996) (*United Distribution Companies*).

product called electric energy and transmission was part and parcel of that product). The FPA clearly reserves the right to regulate retail sales of electric energy to the states. As we explained in the Final Rule, however, in today's markets, and increasingly in the future as more states adopt retail wheeling programs, retail transactions are being broken into products that are being sold separately: transmission and generation. Moreover, these products are being sold increasingly by two or more different entities. For example, a transaction may **[30,340]** involve transmission service from one or more transmission providers who move power from a distant generation supplier, over the interstate transmission grid, to an end user. Because these types of products and transactions were not prevalent in the past, the jurisdictional issue before us did not arise and, contrary to IL Com's argument, the Commission cannot be viewed as "disturbing" the jurisdiction of state regulators prior to and after the Attleboro case.[461]

As we also explained in the Final Rule, the legislative history of the FPA and the relevant case law similarly reflect the historical market structure in which electricity and transmission generally were bought on a bundled basis.[462] Today's unbundled world simply was not contemplated and the cases do not resolve dispositively this jurisdictional issue. The case law focuses primarily on the bright line between wholesale sales and retail sales of energy, and transmission in interstate as opposed to intrastate commerce. It does not

---

[461] *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927).

[462] The case law is addressed extensively in Appendix G to the Final Rule and will not be repeated here.

address unbundled retail interstate transmission.[463] We therefore have interpreted the case law in light of changed circumstances and have relied in the first instance on the plain wording of the statute. We find compelling that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce without qualification; unlike our jurisdiction over sales of electric energy, which section 201 specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission.

Since the time Order No. 888 issued, the D.C. Circuit has addressed a similar issue in interpreting section 1(b) of the NGA, the provision that parallels section 201(b) of the FPA. Under section 1(b), the Commission's jurisdiction does not apply "to the local distribution of natural gas or to the

---

[463] On rehearing, several parties argue that at least one court case, *Wisconsin-Michigan Power Co. v. FPC*, 197 F.2d 472 (7th Cir. 1952), *cert. denied*, 345 U.S. 934 (1953) explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services. The Commission discussed this case in detail in Appendix G to the Final Rule, *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,974-75; *mimeo* at 22-25. As we stated there, the court's interpretation of the legislative history of the FPA was at odds with both the plain words of the statute as well as the language of the House Report on the FPA (H.R. Rep. No. 1318 at p. 27). It also did not mention the Senate Report on the FPA, which clearly recognized jurisdiction over all interstate transmission lines, whether or not a sale of energy is carried by those lines (S. Rep. No. 621 at p. 48). We therefore reject arguments that this single case is in any way dispositive of the issue before us.

facilities used for such distribution." Similarly, under section 201(b) of the FPA, the Commission shall not have jurisdiction, except as specifically provided, "over facilities used for the generation of electric energy or over facilities used in local distribution. . ." In responding to arguments regarding the scope of state authority over "local distribution" of natural gas, the court distinguished between bundled and unbundled sales:

> States have been -- and are still -- permitted to regulate LDCs' bundled sales of natural gas to end-users because those transactions include transportation over local mains and the retail sales of gas. In contrast, states have never regulated the terms and conditions of interstate pipeline transportation. When the gas sales element is severed -- i.e., unbundled -- from the transactions, FERC retains jurisdiction over the interstate transportation component." [*United Distribution Companies*, 88 F.3d at 1153 (footnote omitted) (emphasis in original).]

The court's reasoning is also applicable to and supports our jurisdictional determination in Order No. 888.

Several state commissions point to section 212(h) of the FPA and argue that Congress, in refusing to grant the Commission authority to order retail wheeling, left all jurisdiction over retail transmission to the states. We disagree. What Congress did in section 212(h) was to prohibit us from ordering transmission directly to an ultimate consumer. We readily recognize and respect this prohibition. However, the

ability to order retail **[31,341]** wheeling is a separate issue from whether we have jurisdiction over the rates, terms and conditions of retail wheeling in interstate commerce that is ordered by a state or that is provided voluntarily. Congress, in enacting section 212(h), did nothing to modify our jurisdiction under sections 201, 205 and 206 over the rates, terms and conditions of interstate transmission by public utilities.

Similarly, we reject FL Com's arguments that section 212(g) of the FPA prohibits the Commission from asserting any jurisdiction over unbundled retail transmission. Section 212(g) prohibits the Commission from issuing an order that is inconsistent with any state law that governs retail marketing areas of electric utilities. As we stated in the Final Rule, while our jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. We also reject arguments by the FL Com that this Commission's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. This argument is flatly contrary to the longstanding interpretation of the FPA by the United States Supreme Court.[464]

---

[464] *See FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964) (*Colton* case). IN Com makes a similar argument and opposes "federalization" of retail wheeling within a state's boundaries. We reject this argument on the same basis.

Commission's Seven Factor Test

IL Com argues that the Commission should withdraw its technical test. It contends that retail wheeling jurisdiction should follow function and that the function served by public utility facilities in providing retail service does not change upon the unbundling of service to retail customers. According to IL Com, Commission jurisdiction would extend to the service of delivering electric energy by a public utility to wholesale customers, regardless of the nature and extent of the public utility's facilities used to make that delivery. Similarly, it asserts, state jurisdiction would extend to the service of delivering electric energy by a public utility directly to retail customers, regardless of the nature and extent of the public utility's facilities used to make that delivery.

NARUC argues that the seven-factor test does not result in the bright line discussed in *FPC v. Southern California Edison Company*, 376 U.S. 205 (1964). The facility-by-facility categorization of utility systems on a company-specific basis, it asserts, is hardly consistent with the Court's decision to make case-by-case analysis unnecessary.

OH Com asserts that the seven factors provide no useful insight into the nature of local distribution service. It adds that reliance upon technical tests to determine local distribution lacks legal foundation. It further contends that the jurisdictional bright line established by Congress focuses upon the nature of the transaction, not the functional or technical characteristics of a particular wire, in determining whose jurisdictional authority attaches to a particular transaction and facilities. It concludes that the Commission should adopt the

Ohio-proposed retail marketing area "wheeling in" jurisdictional approach.

PA Com contends that the Commission's seven indicia are not acceptable measures of local distribution and challenges each factor.

NH & MI Coms declare that the criteria for distinguishing transmission facilities from local distribution facilities should not be limited to the seven given in the Rule, but should allow consideration of any other relevant criteria for separating local concerns from matters legitimately federal in nature.

NJ BPU argues that the engineering-driven definition does not resolve many of the hazy areas. To the extent that the seven factors do not reflect or cannot be reconciled with the particular circumstances, it contends that the states may be hamstrung in their ability to make **[30,342]** reasoned decisions that comport with Order No. 888.[465]

Similarly, NY Com argues that five of the seven factors (1, 2, 4, 6,and 7) are not accurate when applied to large metropolitan areas and remote rural areas. It asserts that local distribution facilities are not necessarily close to retail customers and the assumption that local distribution facilities

---

[465] *See also* WI Com (criteria do not appropriately reflect the mixed nature of many facilities in systems that are closely integrated and the application of the criteria to the electric system in Wisconsin would supplant state jurisdiction over a large number of facilities whose primary functions are local reliability and retail service).

are primarily radial in character fails to account for network systems. It adds that reconsignment or transportation of power to different markets can and does occur at the local distribution level. It further adds that the presence of meters is not a discerning characteristic of where interstate transmission ends and local distribution begins; meters are frequently not part of the transmission/local distribution interface. Nor, according to NY Com, are local distribution systems necessarily of reduced voltage. Instead of the 7 criteria, NY Com argues that the Commission should adopt a functional measure of local distribution based on factors 3 and 5 (interstate transmission ends and local distribution begins where electricity flows into a comparatively restricted geographic area and does not flow back out of that area and the power is consumed in that area) and on the traditional classification of the facilities by the state regulatory body (or what the utility has traditionally classified as local distribution).

Commission Conclusion

Several parties on rehearing do not like the seven-factor technical test for local distribution facilities that was set forth in Order No. 888. That test takes into account both technical and functional characteristics of the transaction involved. The parties on rehearing propose instead a variety of bright line tests. For example, IL Com wants state jurisdiction to extend to the "service" of delivering electric energy to retail customers, which it would define to give it jurisdiction regardless of the nature and extent of the facilities used to make the delivery. OH Com proposes that the Commission adopt a retail marketing area "wheeling in"

jurisdictional approach which would give it jurisdiction over facilities within territorial boundaries.

In response, we do not interpret the FPA to permit us in effect to rewrite the statute to give states jurisdiction over interstate transmission services. Moreover, we reject arguments of OH Com that our seven-factor test lacks legal foundation, and arguments of NARUC that we are somehow bound to develop a bright line test. While Congress established a jurisdictional bright line between wholesale and retail sales of energy, there is no such bright line that we can divine with regard to transmission and local distribution facilities. The Supreme Court, in both Colton and CL&P,[466] has instructed us that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. The seven factors will permit us to undertake this fact-specific determination.

We acknowledge the concerns raised by several state commissions that the seven-factor test does not, as NJ BPU puts it, resolve many of the hazy areas, and that there may be other factors that should be taken into account in particular situations. The seven-factor test is intended to provide sufficient flexibility to take into account unique local characteristics and historical usage of facilities used to serve retail customers. We specifically stated in the Final Rule that we will consider jurisdictional recommendations by states that take into account other technical factors that states believe are appropriate in light of historical uses of particular facilities.

---

[466] *See Colton*, 376 U.S. at 210 n.6; CL&P, 324 U.S. at 531-36.

Moreover, we will defer to facility classifications and/or cost allocations that are supported by state regulatory authorities. For example, in the ongoing California electric utility restructuring proceeding, the Commission deferred to the State PUC's recommendations regarding the split between state-jurisdictional local distribution facilities and Commission-**[30,343]** jurisdictional transmission facilities.[467]

Oppose transmission of public utility purchases for sale at retail

IL Com objects to the transmission unbundling requirement if it is intended to require public utilities to take transmission services under their own FERC tariffs for purchases of power intended for distribution by the public utility to retail customers. According to IL Com, a distinction must be made between the public utility's use of its transmission system in cases in which the public utility purchases wholesale power for sale for resale, and cases in which the public utility purchases wholesale power to serve native load retail customers. It argues that the Commission cannot legally regulate, or place conditions on, the manner in which a utility uses its transmission system to make sales of electric energy at retail. It contends that the Commission must exempt public utility power purchases for sale at retail from the unbundling requirement. It recommends that the Commission insert the words "for sale for resale" after the word "purchases" in section 35.28(c)(2) and after the word "purchase" in section 35.28(c)(2)(i).

---

[467] *Pacific Gas and Electric Company, et al.*, 77 FERC ¶61,325 at p. 61,325 (1996).

Commission Conclusion

The Commission rejects arguments of IL Com that if unbundled retail wheeling occurs either voluntarily or as a result of a state retail program, we cannot require the utility to take service under its own transmission tariff for sales to retail customers. This requirement is a term and condition of unbundled retail interstate transmission service and, as explained above, therefore is within our exclusive jurisdiction. Additionally, this should not in any way infringe on state retail programs or service to retail customers. Rather, it ensures that non- discriminatory transmission services are provided to all potential retail power competitors.

Further, as stated previously in Section IV.C.1.b (Transmission Providers Taking Service Under Their Tariff), we clarify that a transmission provider does not have to "take service" under its own tariff for the transmission of power that is purchased on behalf of bundled retail customers.

Oppose buy-sell transaction analysis

PA Com asserts that there is a potential for jurisdictional conflict with respect to buy-sell transactions that is a direct consequence of the technical-functional test (which PA Com challenges).

IL Com argues that states have exclusive authority to regulate buy-sell arrangements as bundled retail sales. It further argues that the Commission cannot make a bundled retail sale into an unbundled retail sale simply by characterizing it as the functional equivalent of an unbundled retail sale; by re-characterizing them the Commission is

effectively ordering the unbundling of buy-sell arrangements. It asserts that buy-sell arrangements on the electric side are not an end run around clear federal jurisdiction and that the Commission should withdraw its assertion of jurisdiction over the retail transmission component of unbundled retail sales.

VT DPS contends that the Commission's rationale is flawed: "FERC's analysis rests on the same very shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies." According to VT DPS, all retail transactions are subject to state jurisdiction and asks the Commission to clarify that the Commission defines buy-sell as it did in the NOPR, but also acknowledge that it has no jurisdiction over such arrangements.

IN Com asserts that in the absence of any record of abusive and undermining actions by states under the guise of buy-sell arrangements, there is not even a remedial justification to touch buy-sell transactions. It contends that a difference between the FPA and the NGA warrants different treatment -- the FPA exempts from FERC jurisdiction local distribution and transmission of electric energy in intrastate commerce. By redefining interstate transmission, IN Com claims that the Commission proposes to do away with the meaning history has accorded to a variety of transactions previously considered wholly intrastate in nature. According to IN Com, states should be allowed **[30,344]** to experiment with and allow different forms of buy-sell transactions as part of the evolving marketplace.

Commission Conclusion

Four parties (PA Com, IL Com, VT DPS and IN Com) have raised concerns regarding the Commission's determination that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third party. The Commission reiterates that we will have to address these situations on a case-by-case basis. We disagree with IL Com that States have exclusive authority to regulate the interstate transmission component of buy-sell transactions. Similarly, we deny the VT DPS request that we acknowledge no jurisdiction over such arrangements. The fact remains that these arrangements could be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. We reserve our authorities to ensure that public utilities and their customers are not able to circumvent non-discriminatory transmission in interstate commerce. In response to VT DPS' contention that the Commission's analysis here rests on the same shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies, we note that the D.C. Circuit recently affirmed the Commission's assertion of jurisdiction over buy/sell arrangements under the Natural Gas Act.[468]

---

[468] *United Distribution Companies*, 88 F.3d at 1154-57.

State jurisdiction over the service of delivering electric energy to end users

Rehearing Requests

IL Com states that it is far from clear what FERC contemplates by the "service" of delivery of electric energy by a delivering utility in the retail wheeling transaction. It is equally unclear to IL Com whether the "service" to which Order No. 888 refers is a public utility activity over which state regulators would have jurisdiction. IL Com argues that it is the Illinois legislature, not FERC, that determines whether IL Com can regulate something called "delivery service."[469]

MO/KS Coms ask the Commission to clarify the meaning of the statement that even when the test for local distribution facilities identifies no local distribution facilities, the Commission believes that states have authority over the service of delivering electric energy to end users. According to MO/KS Coms:

> The authority to shop at retail and to sell at retail do not exist in the FPA. If the Commission's goal is to recognize the States' authority to establish conditions on retail competition, it need only acknowledge the

[469]*See also* AK Com (should not create a fictional concept of delivery service -- the legal reality is that, under retail competition, state law will establish a customer's right to be served and a generation owner's right to produce power. AK Com asserts that the state can then attach conditions to those rights).

> State jurisdiction to establish the opportunity to shop and sell at retail. If this is what the Commission is seeking to accomplish by its discussion of 'delivery service,' then we support the Commission."[470]

Coalition for Economic Competition asserts that the Commission failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, and that the local regulatory commission may have no jurisdiction over either the sale or the transmission of the energy.

Commission Conclusion

Several parties ask us to clarify our conclusion that even when the seven-factor test for local distribution facilities does not identify local distribution facilities, we believe states have authority over the "service" of delivering electric energy to end users. We clarify that states have the authority to determine the retail marketing areas of electric utilities within their jurisdictions, and the end user services that those utilities must provide, but we did not in Order No. 888 intend to opine on the extent of authority given by state legislatures to their state commissions. Rather, our statement regarding state authority over the "service" of delivering electric energy is intended to recognize the historical and local nature of delivering power to end users and the **[30,345]** states' legitimate concerns and responsibilities in regulating local matters.

[470]MO/KS Coms at pp. 1-13.

Deference to states

Rehearing Requests

Support broader deference

NARUC and IL Com argue that the Commission should not simply defer to state recommendations concerning the application of the seven-factor test or the recovery of stranded costs, but should conclusively rely on the findings by state commissions.

NY Com argues that the Commission should not limit deference to instances in which states order retail wheeling, but should defer to all state commission recommendations regarding the definition of local distribution facilities.

FL Com asserts that the Rule fails to say where deference will be given. It argues that the Rule should state that when a state commission has held a proceeding on matters related to the requirements of the Rule, the Commission shall give deference to the state commission decisions. Moreover, it asserts that the Commission should codify the deference standard: "When a state commission has held a proceeding on matters related to the requirements of this rule, the Commission shall give deference to the state commission decisions." (FL Com at pp. 7-9).

The commitment to defer to a state regulatory commission or agency, argues NE Public Power District, should be clarified with respect to utilities located in Nebraska, which has no such commission or agency. NE Public Power District assumes that deference will be accorded

to decisions of NE Public Power District's Board of Directors; if not, it asks the Commission to clarify.

PA Com asks the Commission to clarify what a state regulatory agency must demonstrate to secure deference and to define the term "consult." PA Com states that, in discussing the seven indicia, the Commission states that it will "consider" jurisdictional recommendations by states, which PA Com asserts is much different from deference. It also asserts that the Commission must clarify what it will do if a utility's classifications and/or cost allocations are not supported by state regulatory authorities.

Oppose deference to state authorities

TANC argues that the Commission erred in deferring to state regulatory authorities in drawing jurisdictional lines for local distribution facility classifications and/or cost allocations. According to TANC, the Commission unlawfully and unnecessarily abdicated its jurisdiction under the FPA (citing *New England Power Co. v. New Hampshire*, 455 U.S. 331, and *Nantahala Power and Light Co. v. Thornburg*, 476 U.S. 953). With respect to ISOs, it asserts that the Commission should not defer to state authority in making determinations with respect to classifications of facilities.

Commission Conclusion

In response to NARUC and IL Com's arguments that this Commission should not simply defer to state commissions regarding application of the seven-factor test but instead should conclusively rely on the findings of state commissions, we believe this is inconsistent with the case law which states

that local distribution it is a matter of fact for the Commission to determine as an original matter.[471] Additionally, we have an independent obligation to ensure that we are fulfilling our responsibilities under the FPA to regulate facilities that are used in interstate commerce. We cannot delegate our jurisdiction. However, we intend to provide broad deference to states in determining what facilities are Commission-jurisdictional transmission facilities and what facilities are state-jurisdictional local distribution facilities, so long as our comparability principles are not compromised and we are able to fulfill our responsibilities under the statute.

We reject FL Com's suggestion that we codify the deference standard. This is neither necessary nor appropriate. In response to NE Public Power District's request that we clarify to whom we would give deference in Nebraska, we clarify that because Nebraska does not have an electric regulatory commission or agency, there is no appropriate regulatory entity to whom our deference standard would apply; accordingly, we will address the **[30,346]** transmission/local distribution issue for Nebraska without giving deference to any particular entity. In response to PA Com's request that we clarify what we will do if a utility's classifications and/or cost allocation proposals are not supported by state regulatory authorities, we will make a determination based on the factual record before us in a particular case, taking into account the views of the state regulatory authority.

---

[471] *See Colton and Connecticut Light and Power, supra.*

TANC has argued that we have unlawfully abdicated our jurisdiction by deferring to state recommendations. TANC confuses delegation of jurisdiction, which we cannot do, with willingness to defer to states based on their application of criteria that we have provided. Even in the cases in which the Commission defers to states' views, we will still independently evaluate all material issues and proceed only where substantial evidence supports the states' views. The Commission clearly can entertain requests for deference in these circumstances.

J. *Stranded Costs*

As indicated in our prior discussion in Section IV.A.5, there are two major overlapping transition issues that arise as a result of this rulemaking: stranded cost recovery and how to deal with contracts entered into under the prior regulatory regime. We here address stranded cost recovery and, as in the prior discussion, we believe it is important to explain the general context in which our stranded cost determinations have been made before addressing the various rehearing requests on this issue.

In Order No. 888, the Commission removed the single largest barrier to the development of competitive wholesale power markets by requiring non-discriminatory open access transmission as a remedy for undue discrimination. This action carries with it the regulatory public interest responsibility to address the difficult transition issues that arise in moving from a monopoly, cost-based electric utility industry to an industry that is driven by competition among wholesale power suppliers and increasing reliance on market-based generation rates. The most critical transition issue that

arises as a result of the Commission's actions in this rulemaking is how to deal with the uneconomic sunk costs that utilities prudently incurred under an industry regime that rested on a regulatory framework and a set of expectations that are being fundamentally altered.

The Commission determined in Order No. 888 that it must address stranded costs, and that it must do so at an early stage -- particularly in light of the lessons learned from our experience with similar issues in the natural gas area. We noted that when we did a similar restructuring in the gas industry, the D.C. Circuit invalidated the Commission's efforts precisely because the Commission had failed to deal with the stranded cost problem in a satisfactory manner.[472] We explained that, based on the lesson of AGD, the Commission cannot change the rules of the game without providing a mechanism for recovery of the costs caused by such regulatory-mandated change.

Since the time Order No. 888 issued, we have been provided with additional guidance from the court in the natural gas area, which has further helped to inform our decisions here. In its decision on review of Order No. 636,[473] the D.C. Circuit upheld the Commission's decision to allow the recovery of gas supply realignment costs. In so doing, the court, while questioning a specific feature of the stranded cost recovery mechanism employed in Order No. 636, has

---

[472]*Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988) (*AGD*).

[473]*United Distribution Companies v. FERC*, 88 F.3d 1105 (1996) (*United Distribution Companies*).

nevertheless again reaffirmed the basic principle that stranded cost recovery is an appropriate component of a regulatory policy aimed at accomplishing a fair and reasonable transition to competitive markets. The question as to the Commission's ability to allow the recovery of stranded costs has been laid to rest.

The task before the Commission in this rulemaking is thus to determine how best to meet its responsibility to address the costs of the transition to a competitive industry, particularly insofar as those costs are stranded, or in effect rendered unrecoverable, as a result of the transmission access required by us under the **[30,347]** FPA.[474] As the rehearing arguments demonstrate, there is no consensus on how the Commission should address the stranded cost issue. In fact, petitioners are at polar extremes as to what the Commission should do regarding stranded costs. Some argue that the Commission has gone too far in permitting utilities to seek recovery of stranded costs, whether such costs are associated with wholesale requirements contracts, with retail-turned-wholesale customers, or with retail customers that obtain retail wheeling.[475] Others argue that the Commission has not

---

[474]Such access may be the open access required under this Rule or case-by-case transmission access ordered pursuant to FPA section 211.

[475]We note that the regulations implementing this Rule use "wholesale stranded cost" and "retail stranded cost" as shorthand terms to refer to the different situations in which a utility may experience stranded costs. However, as the definitions of those terms make clear, it is not the nature of the costs (wholesale vs. retail) that is controlling for purposes of stranded cost recovery

gone far enough and that it must broaden the scope of stranded cost recovery permitted under the Rule. Indeed, some would have us be the guarantor for recovery of all uneconomic costs that might be stranded in the move to more competitive markets, no matter how tenuous the nexus to this Rule, and irrespective of state-Federal jurisdictional complexities. Some support the Commission's decision to recover stranded costs directly from the departing customers. Others would prefer that the Commission require utilities to absorb a portion of their stranded costs or that the Commission spread the burden of stranded costs among all of the utility's customers. Some object that the Commission's approach to stranded costs in the electric industry is different from that adopted in the gas industry. Some entities support the Commission's revenues lost approach for measuring a departing customer's stranded cost obligation. Others propose different methods for computing stranded costs.

Given the plethora of positions that entities have raised both initially and on rehearing concerning stranded costs, the Commission has taken a careful, measured approach with regard to stranded cost recovery. The Commission has balanced a number of important interests in order to achieve what it believes will be a fair and orderly transition to

---

under this Rule. Rather, the controlling factors are the status of the customer (wholesale transmission services customer vs. retail transmission services customer) with whom the costs are associated, and whether the transmission tariffs used by the customer to escape its former power supplier (thus causing the stranding of costs to occur) were required by this Commission or by a state commission. As a result, "retail stranded costs" refers to stranded costs associated with retail wheeling customers.

competitive markets. These interests include the financial stability of the electric utility industry, upholding the regulatory bargain under which utilities made major capital investments, and not shifting costs to customers that had no responsibility for causing those costs to be incurred. The Commission also has adopted an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of stranded cost recovery from retail customers, recognizes state commission jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures.

The balancing of interests and considerations described above is reflected in the following central components of the Rule's stranded cost provisions, which are reaffirmed herein.[476] First, the Commission has determined that the most reasonable, legally supportable approach is one that permits utilities to seek recovery of wholesale stranded costs under this Rule (whether the stranded costs are associated with a departing wholesale requirements customer or with a retail-turned-wholesale customer) only in those cases in which there is a *direct nexus* between the availability and use of Commission-required transmission access[477] and the **[30,348]**

---

[476]We reaffirm below our basic determinations, but make certain clarifications on limited issues and grant rehearing on the municipal annexation issue.

[477]As we explain below, by "Commission-required transmission access" we mean the open access transmission required under this Rule or required pursuant to a section 211

stranding of costs. In order for the utility to be eligible to seek recovery of stranded costs from a departing customer, the customer must have obtained access to a new generation supplier through the use of the former supplying utility's Commission-required transmission tariff (i.e., its open access tariff or a tariff ordered pursuant to FPA section 211), not through the use of another utility's transmission system.

Other cost recovery issues are more appropriately addressed outside the context of this Rule. For example, the Rule is not intended to apply to costs associated with the normal risks of competition, such as self-generation, cogeneration, or loss of load, that do not arise from the new, accelerated availability of Commission-required transmission access. If a customer leaves its utility supplier by exercising options that could have been undertaken prior to mandatory transmission under Order No. 888 or the Energy Policy Act, or that do not rely on access to the former seller's transmission, there is no direct nexus to Commission-required transmission access and thus no opportunity for stranded cost recovery under the Rule.

Second, the Commission has limited the opportunity to seek stranded cost recovery under the Rule primarily to two discrete situations: (1) costs associated with customers under wholesale requirements contracts executed on or before July 11, 1994 (referred to in the Rule as "existing wholesale

---

order, as well as transmission provided prior to Order No. 888 (and not pursuant to a section 211 order) where such transmission was provided on a case-by-case basis to comply with the Commission's comparability requirement. *See* note 484 *infra*.

requirements contracts") that do not contain an exit fee or other explicit stranded cost provision; and (2) costs associated with retail-turned-wholesale customers. With regard to the existing wholesale requirements contracts, the Commission also has made a finding that it is in the public interest to permit amendments to add stranded cost provisions to these contracts, even if they contain *Mobile-Sierra* clauses, if case-by-case evidentiary burdens are met. We do not interpret the *Mobile-Sierra* public interest standard as practically insurmountable in extraordinary situations such as this one where historic statutory and regulatory changes have converged to fundamentally change the obligations of utilities and the markets in which they and their customers will operate.

Third, Order No. 888 *does not guarantee* that a utility will be allowed to recover stranded costs. Rather, it provides an opportunity for such recovery. To be eligible to recover stranded costs from a departing customer in a particular case, the utility must demonstrate that it incurred costs to provide service to the customer based on a reasonable expectation of continuing service to that customer beyond the contract term.[478] In the case of stranded costs associated with wholesale requirements contracts customers, if the contract contains a notice of termination provision, that provision is strong evidence that the parties were aware that at some point in the future the customer might seek to find another supplier.

---

[478]We have made a minor revision to the regulatory text, section 35.26(c)(2), to conform the language of that section with sections 35.26(b)(1) and (5). A conforming revision has been made to section 35.26(d)(2)(i).

Therefore, there is a rebuttable presumption of no reasonable expectation, and therefore no opportunity for stranded cost recovery unless the utility can overcome the presumption.

The Commission has concluded that direct assignment of stranded costs to the departing customer (through either an exit fee or a surcharge on transmission) is the appropriate method for recovery of stranded costs under the Rule. In reaching this conclusion, the Commission carefully weighed the arguments supporting direct assignment of stranded costs against those supporting a more broad-based approach, such as spreading stranded costs to all transmission users of a utility's system, and also took into account the fact that we applied a different approach in the natural gas area. The central considerations that support a direct assignment approach in the electric industry are that the approach follows the traditional regulatory concept of cost causation, it avoids shifting costs to customers that had no responsibility for causing them to be incurred or for causing them to be stranded, and it is still possible to apply such an approach at this stage of the industry's evolution.

[30,349]

There is no question that, without the stranded cost recovery mechanism, some customers would be far more likely to switch to lower-cost suppliers and enjoy sooner the benefits of a competitive power market. But, as detailed in Order No. 888, such an approach may result in higher costs for other customers. We thus have had to balance the potential for earlier benefits for some customers against other public interest considerations, most particularly the need to provide a fair mechanism by which utilities can recover the costs of past investments under traditional regulatory concepts of

prudently incurred costs and cost causation. The result is not to deny competitive advantages, but only to delay their full realization for some customers so that all customers ultimately will benefit.

While Order No. 888's cost causation approach is different from the Order No. 636 cost spreading approach that was affirmed in the *United Distribution Companies* case, we believe it is the preferable approach given the early stage of the electric utility's competitive transition. We do not read the court's opinion as precluding the Commission from adopting a direct assignment approach in Order No. 888, particularly where, as here, the Commission has fully explained and justified the reasons for following traditional cost causation principles. In addition, although the *United Distribution Companies* court remanded for further consideration (in light of Order No. 636's cost spreading approach) the decision not to require any pipeline absorption of gas supply realignment costs, the Commission has fully explained how its decision in Order No. 888 not to require any utility absorption of stranded costs is consistent with its decision to follow traditional cost causation principles. With respect to the fundamental conclusion that utilities should be permitted an opportunity to recover their prudently incurred costs, Order No. 888 is fully consistent with Order No. 636. Although the Commission in Order No. 888 chose a direct assignment method (rather than the cost-spreading approach in Order No. 636) for purposes of allocating stranded cost responsibility among customers, the approach used by the Commission in Order No. 888 is not governed by decisions in Order No. 636, but in either event the Commission must demonstrate that its choice of methods is based on reasoned decision-making.

In considering the stranded cost issues that may arise in the transition to competitive markets, the Commission also has taken cognizance of significant changes involving retail customers and the stranded cost issues that arise as retail customers convert to wholesale customer status (*e.g.*, through municipalizations) in order to obtain the open access afforded by Order No. 888, or as they obtain retail wheeling required by state commissions. These situations involve new and complex jurisdictional issues and represent the bulk of potential stranded costs facing the industry. We believe it is important to clarify the Commission's decisions as to when it will entertain requests for stranded cost recovery in these situations, and our reasons for doing so.

The Commission's determination that it, rather than the states, should be the primary forum for addressing stranded costs associated with a retail-turned-wholesale customer[479] is limited to those cases in which there is a *direct*

---

[479]In Order No. 888 and here, we sometimes use the shorthand expression "retail-turned-wholesale" customer. By this we do not mean that a retail customer who is an ultimate consumer ceases to be an ultimate consumer, or that this customer begins to purchase electric energy for resale. Rather, in a "retail-turned-wholesale customer" situation, such as the creation of a municipal utility system, a newly- created entity becomes a wholesale power purchaser on behalf of retail customers who were formerly bundled customers of the historical local utility power supplier. The new municipal utility is the conduit by which retail customers, if they cannot obtain direct retail access, can reach power suppliers other than their historical local utility power supplier. Although the retail customers remain bundled retail customers, in that they become the bundled customers of the new entity, we call this a "retail-turned-

nexus between the availability and use of Commission-required transmission access and the stranding of costs. We believe we have both the authority and the obligation to provide an opportunity stranded cost recovery in these situations because the bundled retail customer would not be able **[30,350]** to obtain access to the new supplier *but for* the Commission's order requiring transmission. The creation of a new wholesale entity to purchase power on behalf of retail customers would not, by itself, trigger stranded costs. IN the absence of transmission access from the historical supplier of the retail customers, the new entity would have to remain on the historical supplier's generation system because it would have no way to reach other power suppliers and stranded costs would not occur.[480] Therefore, there is a causal nexus between the stranded costs and the availability and use of the tariff services *required by the Commission*.[481] Moreover, because of

---

wholesale customer" situation because the new entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply.

[480]Exceptions would be self-generation or construction by the new entity of its own transmission line, in which case, as noted earlier, the stranded cost provisions of Order No. 888 would not apply because such options have always been available as alternatives to purchasing power from the historical supplying utility and do not involve the use of the utility's transmission facilities under an open-access tariff. Thus the departure of customers under these circumstances cannot be linked to the open-access requirements of this Rule.

[481]As discussed in greater detail in sections IV.J.6 and IV.J12 below, we clarify that the opportunity for recovery of stranded costs in a retail-turned-wholesale situation is limited to

this causal nexus between the use of a jurisdictional utility's Commission-required transmission tariff and the potential for foregone revenues by that jurisdictional utility as a result of the Commission-required access, the stranded costs associated with a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In contrast, in the situation in which a bundled retail customer obtains retail wheeling, stranded costs are directly caused by the availability and use of unbundled retail services *required by the state commission*, not this Commission.[482] Thus, the Commission believes that states, not the Commission, should be the primary forum for costs associated with a bundled retail customer that obtains retail wheeling. The Commission's decision to entertain requests to recover stranded costs caused by retail wheeling in *only* a limited circumstance (where the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on a policy decision

---

cases in which the former bundled retail customer subsequently becomes, either directly or through another wholesale transmission purchaser, an unbundled wholesale transmission services customer of its former supplier. We have revised section 35.26(b)(1)(i) of the Commission's regulations accordingly.

[482]Unbundled retail transmission services required by a state commission could be taken under the same *pro forma* open-access tariff sued by wholesale customers or, if determined appropriate by the Commission, under a separate retail tariff filed at the Commission. The critical point, however, is that in either case, the unbundled services are required by the state and not by this Commission.

by the Commission that it will step in to fill a regulatory "gap" that could result in no effective forum in which utilities would have an opportunity to seek recovery of prudently incurred costs.

Finally, after considering various proposals regarding how stranded costs should be calculated, and reviewing the arguments of petitioners on rehearing, the Commission continues to believe that the revenues lost approach is the fairest and most efficient way to determine the amount of stranded cost assigned to a departing customer during the transition to a competitive wholesale bulk power market. The Commission has rejected an asset-by-asset approach as overly complicated and costly.

We respond below to the specific arguments raised on rehearing and elaborate on the above determinations.

* * * * *

[pp. 30,402-30,424]

[30,402]

6. Recovery of Stranded Costs Caused by Retail- Turned-Wholesale Customers

In Order No. 888, we concluded that this Commission should be the primary forum for addressing the recovery of stranded costs caused by a retail-turned-wholesale customer.[672]

---

[672]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,818-19; *mimeo*

We stated that if such a customer is able to reach a new generation supplier because of the new open access (through the use of a FERC-filed open access transmission tariff or through transmission services ordered pursuant to section 211 of the FPA), any costs stranded as a result of this wholesale transmission access should be viewed as "wholesale stranded costs." We explained that there is a clear nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs and that, in these circumstances, this Commission should be the primary forum for addressing recovery of such costs.[673]

We said we will not be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory. We indicated that in these situations there is no direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs. The risk of an existing municipal utility expanding its territory was a risk prior to the Energy Policy Act and prior to any open access requirement.

Nevertheless, we did express concern that there may be circumstances in which customers and/or utilities could

---

at pp. 534-37.

[673]We indicated that we will require the same evidentiary demonstration for recovery of stranded costs from a retail-turned-wholesale customer (and will apply the same procedures for determining stranded cost obligation) as that required in the case of a wholesale requirements customer.

attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission -- either this Commission or state commissions -- to address recovery of stranded costs. We reserved the right to address such situations on a case-by-case basis.

Rehearing Requests Opposing Retail-Turned-Wholesale Jurisdiction

A number of entities challenge the Commission's assertion that costs associated with retail-turned-wholesale customers would not be stranded but for the FERC-jurisdictional transmission access requirement. They assert that the condition precedent to municipalization is the operation of a state process, and thus that it cannot be the case that the recovery of costs caused by a retail-turned-wholesale customer is "not subject to regulation by the States." They submit that such costs would not be stranded but for the action of state legislators or state regulators in granting authority for the customer's status change. They argue that any nexus that the Commission's authority under the FPA has to wholesale transmission services subsequently provided to the new **[30,403]** wholesale customer is entirely derivative of the state's action.[674]

A number of entities argue that jurisdiction over costs that are stranded when a retail customer becomes a wholesale customer should be left to the states because the facilities used to provide retail service to these retail customers were subject

---

[674]*E.g.*, NARUC, TAPS, Nucor, Suffolk County, IL Com, Multiple Intervenors, APPA, CAMU, WI Com, NASUCA.

to state jurisdiction and were included in retail rate base when the service was rendered.[675] They argue that because the Commission had no jurisdiction over the public utility facilities and costs incurred to serve retail-turned-wholesale customers, it has no jurisdiction to address those public utility costs if they become stranded. Thus, according to these entities, the conversion of the customer from retail to wholesale does not simultaneously effectuate a conversion of the costs from retail to wholesale.

AR Com and MO/KS Coms submit that jurisdiction over the costs incurred for historical retail customers does not shift unless the parties themselves make those costs a part of their new wholesale contract. NY Com submits that the Commission should recognize the states' jurisdiction to set the level of stranded costs associated with retail-turned-wholesale customers to be recovered in wholesale transmission rates set by FERC. FL Com asserts that state authorities are in a better position to assess the extent of stranded facilities and their costs, and that the Commission's involvement should be limited to that requested by a state by petition.

OH Com states that the Commission's position on stranded costs associated with retail-turned-wholesale customers invites second-guessing of state commission determinations and encourages forum shopping by introducing more than one stranded cost treatment within a single state jurisdiction. It expresses concern that utilities may seek to

---

[675] *E.g.*, ELCON, IL Com, IN Com, American Forest & Paper, AR Com, MO/KS Coms, NJ BPU, Suffolk County, WY Com, VA Com, FL Com, NARUC, TAPS.

creatively disaggregate into generation, transmission, and distribution companies in ways to deliberately recast traditional retail relationships as wholesale in an effort to obtain favorable regulatory treatment of stranded costs.

IN Com submits that Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers will discourage state legislatures from making municipalization more available. VT DPS and Valero argue that the threat of a stranded cost surcharge will erect a new barrier to the formation of municipal utilities. They note that the Rule refers to one commenter's observation that, if *Otter Tail* could have made a stranded cost claim against the municipal utility that Elbow Lake planned to create, *Otter Tail* would not have needed to refuse to wheel and there would never have been an *Otter Tail* case. They submit that the Commission never addressed whether, or why, it believed the point to be wrong.

VT DPS and Valero also assert that the Rule represents a major inconsistency with prior Commission treatment of municipalization. They submit that the Commission historically promoted franchise competition between municipalities and utilities by holding tariff provisions that restrict such competition to be anticompetitive and unreasonable.[676]

---

[676] VT DPS and Valero cite in this regard *Florida Power & Light Company*, 8 FERC ¶61,121 (1979); *Power Authority of the State of New York v. FERC*, 743 F.2d 93 (2d Cir. 1984); *Metropolitan Transportation Authority v. FERC*, 796 F.2d 584 (2d Cir. 1986).

American Forest & Paper submits that recovery of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's actions in the natural gas industry, where the Commission has encouraged competition at the retail level through competitive bypass and has not created barriers to competitive entry by imposing transition charges or exit fees on converting customers.[677]

Nucor objects that the Rule does not address the substantive findings, the common sense rationale, or the jurisdictional distinction drawn in *United Illuminating*.**[30,404]**[678] It contends that the Commission's observation in Order No. 888 that there may not be a state regulatory forum for the recovery of stranded costs associated with retail-turned-wholesale customers and hence that the Commission should be the primary forum for addressing such stranded costs is flawed because there always is a state forum to address such cost recovery (the adequacy of the relief provided is a very distinct issue) and open access transmission does not and cannot cause retail competition to occur.[679]

---

[677]American Forest & Paper cites in support of its position Great Lakes Gas Transmission Limited Partnership, 68 FERC ¶61,376 (1994).

[678]*United Illuminating Company*, 63 FERC ¶61,212, *reh'g denied*, 64 FERC ¶61,087 (1993) (*United Illuminating*).

[679]*See also* Suffolk County Rehearing (Commission's analysis in *United Illuminating* was correct; nothing has changed to warrant the Commission's rejection of that analysis).

Commission Conclusion

We will reject the requests for rehearing of our decision to be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers. We find the requests for rehearing on this issue unpersuasive. While it may be the case, as some entities suggest, that state action is a condition precedent to municipalization, the rehearing petitions ignore the fact that the Rule covers situations in which open access is also a condition precedent to the municipalized customers leaving their existing supplier's system. Order No. 888 does not propose that the Commission be the primary forum for stranded cost recovery for all cases of municipalization. Instead, our holding is limited to those cases in which the new wholesale entity uses Commission-mandated transmission access to obtain new power supply on behalf of retail customers that were formerly supplied power by the utility providing the transmission service.[680]

As we explained in Order No. 888, in such cases there is a direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of costs stranded as a result of this wholesale transmission access. Thus, the stranded costs associated with

---

[680]In the case of municipalization, the bundled retail customers of a local utility become the bundled retail customers of the new municipal utility. As explained above, we call this a "retail-turned-wholesale customer" situation because the new municipal entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply.

retail-turned-wholesale customers for which Order No. 888 provides an opportunity for recovery would not have been incurred but for the action of this Commission in requiring a utility to make unbundled transmission services available. In these cases, the former bundled retail customers of the historical supplying utility (now the bundled retail customers of the new municipal system) would not have obtained access to new power supply but for the Commission's order mandating transmission. Without the regulatory mandate to provide access, the utility would have indirectly continued sales to the same retail customers because the new municipal utility purchasing power on the retail customers' behalf would have had no way to reach other power suppliers. In this situation, there would be no stranded generation costs. In other words, the creation of a municipal utility intermediary to purchase power at wholesale would not, by itself, trigger stranded costs. Rather, it is the access from the historical supplier of the bundled retail customers that is the condition precedent to reaching other power suppliers and thereby triggering stranded costs. Therefore, there is a clear causal nexus between the stranded costs and the availability and use of the tariff required by the Commission.

Costs that are exposed to nonrecovery when a retail customer or a newly-created wholesale power sales customer ceases to purchase power from the utility and does not use the utility's transmission system to reach a new generation supplier (*e.g.*, through self-generation or use of another utility's transmission system) do not meet the definition of "wholesale stranded costs" for which the Rule provides an opportunity for recovery. Such costs are outside the scope of the Rule because such costs would not be stranded as a direct result of the new open access.

In response to the argument that conversion of a customer from retail to wholesale would not simultaneously effectuate a conversion of the costs from retail to wholesale, we believe this argument confuses **[30,405]** the issue. We note that we have defined stranded costs as wholesale or retail on the basis of whether wholesale or retail open access is the cause of the costs being stranded, not on the basis of the original retail or wholesale characteristic of the costs. Thus, even though costs may have been originally incurred as retail-related costs, the precipitating event that results in such costs being stranded in the retail-turned-wholesale customer scenario is the use by the new wholesale customer of the Commission-mandated tariff. When a customer is able to use the Commission-required tariff to reach another generation supplier, it causes the utility to incur an economic cost in providing transmission service that is equal to the foregone revenues that the utility reasonably expected to receive under a state regulatory regime. Thus, because of the causal nexus between the use of a former supplying utility's Commission-mandated transmission tariff and the potential for foregone revenues by that utility as a result of the Commission-required access, the costs stranded by a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In response to those entities that express concern that the Commission's position on stranded costs associated with retail- turned-wholesale customers invites second-guessing of state commission determinations, we emphasize that we have assumed primary authority to address such costs only in a limited category of cases where there is a direct nexus between the availability of Commission-required open access and the stranding of costs when the former customer uses the

former supplying utility's transmission system (through its open access tariff or a section 211 order) to reach a new supplier. We indicated in Order No. 888 that if the state has permitted any recovery from departing retail-turned-wholesale customers, such amount will not be stranded for purposes of this Rule. We will deduct that amount from the costs for which the utility will be allowed to seek recovery under this Rule from the Commission. In so doing, however, we are not second-guessing the states as to what a utility may recover under state law. Additionally, we will give great weight in our proceedings to a state's view of what might be recoverable.

We also reject the argument that the Commission's position on stranded costs associated with retail-turned-wholesale customers encourages forum shopping. To the contrary, as we said in Order No. 888, to avoid forum shopping and duplicative litigation of the issue, we expect parties to raise claims before this Commission in the first instance. We believe that this Commission should be the primary forum because, without the open access provided by the Rule, the new municipal utility would not be able to reach a new supplier and, as a result, would not cause the utility to incur stranded costs (as defined in this Rule).

We reject as misplaced arguments that the Rule represents a major inconsistency with the Commission's historical promotion of franchise competition between municipalities and utilities and that it will discourage municipalization.[681] It continues to be the Commission's

---

[681] In response to VT DPS and Valero, we note that whether or not Otter Tail may have agreed to wheel power for the municipal

policy to encourage competition. Indeed, the goal of Order No. 888 is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers. However, the purpose of the stranded cost policy is neither to encourage nor to discourage municipalization, but rather to facilitate a fair transition to competition and to ensure stability in the industry during that transition. As we discuss elsewhere in order, we believe that this Commission must address the recovery of the costs of moving from a monopoly-regulated regime **[30,406]** to one in which all sellers can compete on a fair basis and in which electricity is more competitively priced. On this basis, we believe that if a new wholesale entity such as a municipal utility uses Commission-required open access to reach a new supplier on behalf of its retail customers (previously retail customers of the former supplier), the former supplying utility should be given an opportunity to recover legitimate, prudent and verifiable costs that it incurred under the prior regulatory regime to serve that customer.

---

utility that Elbow Lake planned to create if Otter Tail could have made a stranded cost claim against that municipal utility is of no moment to the Commission's decision in Order No. 888 to allow utilities the opportunity to seek recovery of stranded costs associated with retail- turned-wholesale customers. The Court in *Otter Tail* did not address the stranded cost issue because it was not presented in that case. Nor was the Court presented with the extraordinary circumstances -- the historic statutory and regulatory changes, including the requirement of open access, that have converged to fundamentally change the obligations of utilities and the markets in which they operate -- that have justified this Commission's Order No. 888 stranded cost policy.

In response to American Forest & Paper's argument that recovery of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's policy in the natural gas industry of allowing competitive bypass without imposing transition charges or exit fees on converting customers, we note that industrial gas customers who bypass a local distribution company's (LDC) facilities do not escape transition costs quite so easily as suggested by American Forest & Paper. It is true that, when the end user bypasses the LDC to reach an interstate pipeline different from the pipeline serving the LDC, the Commission views the bypass as a risk of competition from which the LDC should not be shielded.[682] However, when the end user bypasses the LDC to reach the same interstate pipeline that serves the LDC, the Commission may take certain actions to minimize adverse effects on the LDC and its remaining customers.[683] Moreover, an end user that bypasses an LDC to reach the same pipeline that serves the LDC would, in any event, be allocated a share of the pipeline's gas supply realignment costs (if any), since those costs are allocated based on current contract demand (or usage).[684] Accordingly, we see no inconsistency between our

---

[682]Texas Gas Transmission Corporation, 65 FERC ¶61,275 (1993).

[683]*Texas Gas Transmission Corporation*, 69 FERC ¶61,245, *reh'g*, 70 FERC ¶61,207 (1995) (requiring pipeline to offer LDC a reduction in its contract demand).

[684]*See Southern Natural Gas Company*, 75 FERC ¶61,046 at p. 61,158 (1996); *Arcadian Corporation v. Southern Natural Gas Company*, 67 FERC ¶61,176 at p. 61,538 (1994). *See also United Distribution Companies*, 88 F.3d at 1181. As the *United*

bypass policy for the natural gas industry and Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers. Similar to our refusal to shield LDCs from the adverse effects of an end user's bypass to reach a different pipeline than serves the LDC, Order No. 888 does not provide an opportunity for stranded cost recovery where a retail-turned-wholesale customer uses another utility's transmission system to reach a new supplier. As we note above, the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers is limited to those cases in which the former retail customer obtains (either directly or through another wholesale transmission purchaser) unbundled transmission services from its former supplying utility. In the case of an end use customer bypassing the LDC to reach the same pipeline that serves the LDC, the end use customer would similarly be allocated a share of the pipeline's gas supply realignment costs. As a result, American Forest & Paper's attempt to rely on the Commission's gas bypass policy is misplaced.

We also disagree with those entities that argue that the Commission has failed to adequately distinguish Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers with the Commission's decision in *United Illuminating*. As we stated in Order No. 888, we recognize that we took a different approach to stranded cost recovery associated with retail-turned-wholesale customers in

---

Distribution Companies court noted, the Commission has given an LDC relief (and required the bypassing customer to bear its share of transition costs) if the LDC can show a direct nexus between the bypass and the pipeline, although the Commission has declined to adopt a generic rule addressing this issue. 88 F.3d at 1180-81.

United Illuminating, where we suggested that state and local regulatory authorities or the courts should be able to provide an adequate forum to address retail franchise matters, including recovery of stranded costs caused by municipalization, but said we would consider revisiting the question if United Illuminating could demonstrate the lack of a forum.[685] However, we explained that since the issuance of that decision we have had an opportunity to re-analyze the nature of the stranded cost problem when a retail customer **[30,407]** becomes a wholesale customer, including the potential that there might not be a state regulatory forum for recovery of such costs. In these circumstances, we have determined that where such costs are stranded as a direct result of Commission-mandated wholesale transmission access, these costs should be viewed as costs of the transition to competitive wholesale bulk power markets and this Commission should be the primary forum for addressing their recovery.

In response to Nucor's objection that there always is a state forum to address stranded cost recovery associated with retail-turned-wholesale customers, with the adequacy of the relief being a distinct issue, we clarify that our primary concern in retail-turned-wholesale situations is not whether there is an adequate state regulatory forum for the recovery of stranded costs associated with retail-turned-wholesale customers. Rather, our primary concern is that wholesale customers (whether or not formerly retail) should be responsible for the costs incurred to meet their power needs that are stranded when they use the wholesale transmission

---

[685]63 FERC at pp. 62,583-84.

ordered by this Commission to reach new suppliers. Our decision to be the primary forum in the case of stranded costs associated with retail-turned-wholesale customers is based on the causal nexus between regulatory- mandated wholesale transmission access and the stranding of costs when a new municipal utility uses such access to obtain new power supply on behalf of retail customers previously served by the former supplying utility.

Rehearing Requests Seeking Expansion of Retail-Turned-Wholesale Jurisdiction

Other entities seek rehearing of the Commission's decision not to be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory.[686] A number of them argue that the loss of existing retail customers through municipal annexations or expansions is no different from the loss of retail customers through new municipalization because existing municipal systems are likely to use Commission-jurisdictional open access transmission to obtain resources to supply power to the annexed loads.[687] They submit that, just

---

[686]*E.g.*, EEI, SoCal Edison, Centerior, Atlantic City, PSE&G, Puget, Public Service Co of CO, Coalition for Economic Competition.

[687]*E.g.*, EEI, SoCal Edison, PSE&G, Puget, Public Service Co of CO, Coalition for Economic Competition. Coalition for Economic Competition suggests, for example, that villages and large industrial customers may opt to join existing municipal systems that, in most cases, will use Commission-jurisdictional

as with newly-municipalized customers, such costs would not be stranded but for the action of this Commission.

Some of these entities express concern that the Rule will encourage retail-turned-wholesale transactions to be undertaken as annexations rather than through the formation of new entities to avoid stranded costs.[688] Public Service Co of CO contends that Order No. 888, in conjunction with the Commission's section 211 order in American Municipal Power Ohio, Inc.,[689] may facilitate municipal annexations by enabling municipal systems to serve new territory through the establishment of second delivery points.

Coalition for Economic Competition and Puget also argue that the Commission must consider stranded costs that arise from municipal expansion in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. They contend that there is no justification for charging one rate to former retail customers taking transmission services through a new municipal utility and another rate to those taking service through municipal annexation or through use of another utility's transmission system.

---

transmission tariffs to obtain resources to supply power to the annexed loads.

[688] *E.g.*, EEI, Coalition for Economic Competition, Atlantic City, Puget, Public Service Co of CO.

[689] 74 FERC ¶61,086, *final order directing transmission service*, 76 FERC ¶61,265 (1996).

PSE&G suggests that the distinction between new municipalization on the one hand and municipal annexation or expansion on the other hand may lead to unnecessary controversy and litigation as entities wrangle over whether a given expansion/annexation is really an expansion or a municipalization. It says that a situation could arise where a municipality **[30,408]** serves one town in order to serve thousands of additional customers in a second town. According to PSE&G, it is not clear from the Rule whether the Commission would consider this an expansion of a municipality's service territory or a new municipalization.

Puget submits that the stranded cost recovery mechanism must not be subject to being frustrated by simple artifices such as having the new supplier (instead of the departing customer) request and contract for transmission service. SoCal Edison seeks clarification of the Commission's authority to mandate stranded cost recovery if a retail customer disconnects from a utility's system and accesses another generation supplier by interconnecting with a public power entity (who in turn would interconnect with a neighboring jurisdictional utility). It asks the Commission to clarify that such a transaction effectively constitutes a municipalization, not an expansion of a service territory, and that the Commission, under FPA section 211, can compel the recovery of stranded costs by having the "new" jurisdictional utility assess a stranded cost charge and pass the revenues on to the utility from whose system the customer departed.

SoCal Edison seeks several additional clarifications. It states that it understands that the Commission's primary forum status in no way prevents or interferes with a state's authority to order stranded cost recovery from departing retail

customers. If this is not the case, SoCal Edison seeks rehearing on this issue. SoCal Edison also asks the Commission to clarify that the Commission retains the discretion to defer to a state stranded cost calculation methodology if appropriate to do so on the facts of a particular case.

Commission Conclusion

We have carefully reviewed the arguments made by petitioners seeking rehearing of our decision not to be the primary forum for stranded cost recovery in the case of municipal annexations. Based on that review we have decided to reconsider our decision. This conclusion is based in large part upon the very significant similarities between the creation of a *new* municipal utility system (also referred to as municipalization) and the expansion of an *existing* municipal utility system (*e.g.*, through annexation of additional retail service territory). We recognize that the *same nexus* to Commission-required transmission access that forms the basis for our decision to allow a utility to seek stranded cost recovery in cases of new municipalization -- use of the former supplying utility's transmission system -- is likely to be present in some cases of municipal annexation. In the case of both new municipalizations and annexations, the bundled retail customers of a local utility become the bundled retail customers of a municipal utility (in one case a new municipal utility, in the other an existing municipal utility) that *will use the transmission system of the retail customers' former supplier in order to access other suppliers*.

As we explain above, in a "retail-turned-wholesale customer" situation, such as the creation of a municipal utility

system, a Docket Nos. RM95-8-001 and RM94-7-002 newly-created entity becomes a wholesale power purchaser on behalf of the retail customers. It is the conduit by which retail customers, if they cannot obtain direct retail access, can reach power suppliers other than their historical local utility power supplier. Although the retail customers remain bundled retail customers, in that they become the bundled customers of the new entity, we call this a "retail-turned-wholesale customer" situation because the new entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply. The same analogy applies to newly-annexed customers; they become "new" wholesale customers in the sense that the wholesale entity obtains transmission and new power supply on their behalf.

Accordingly, we clarify that this Commission will be the primary forum for addressing the recovery of stranded costs if an existing municipal utility uses the transmission system of its annexed retail customers' former supplier to access new suppliers to serve the annexed load. As long as Commission-required transmission access (the former supplier's open access tariff or transmission services ordered under FPA section 211) is the vehicle that enables an existing municipal utility to obtain power supplies to serve annexed loads, we believe that any costs stranded as a result of this wholesale transmission access are properly viewed as economic costs that are jurisdictional to this Commission. **[30,409]** In such a case, the bundled retail customers that are annexed by an existing municipal utility would, through the municipal utility, use the transmission system of their former supplier to obtain access to new supplies and thereby expose their former supplier to non-recovery of prudently incurred costs. As in the case of new municipal systems that use the

transmission system of their retail customers' former supplier, such costs would not be stranded *but for* the action of this Commission in requiring a utility to make unbundled transmission services available.[690]

Just as we will not be the primary forum for stranded cost recovery for all new municipalizations, so also we will not be the primary forum for stranded cost recovery for *all* cases of municipal annexation. Instead, our holding is limited to those cases in which the existing municipal system uses Commission-mandated transmission access from the annexed customers' former supplying utility to obtain power from a new supplier. Costs that are exposed to nonrecovery when an existing municipal utility does not use the transmission system of the retail customers' former supplier to reach a new generation supplier (*e.g.*, through self-generation or use of another utility's transmission system) do not meet the

---

[690]SoCal Edison requests clarification that a transaction in which a retail customer disconnects from a utility's system and accesses another generation supplier by interconnecting with a public power entity, who in turn would interconnect with a neighboring jurisdictional utility, constitutes a municipalization, not an expansion of a service territory. Because we have decided to treat municipal annexations (or expansions) and new municipalizations similarly for purposes of stranded cost recovery under the Rule, SoCal Edison's request is moot to the extent that it envisions a scenario in which the former supplier's transmission system is used to access a new generation supplier. However, as discussed below, the Rule would not provide an opportunity to seek recovery of stranded costs if the municipal entity in the scenario described by SoCal Edison *does not* use the former supplier's transmission system.

definition of "wholesale stranded costs" for which the Rule provides an opportunity for recovery. Such costs are outside the scope of the Rule because such costs would not be stranded as a direct result of Commission-required transmission access.

We reject as misplaced the argument that the Commission, by failing to address costs that arise if a municipal utility (whether a new municipal utility or an existing municipal utility that annexes additional retail customer territory) does not use the historical supplying utility's transmission system, has not met its statutory obligation to "set just and reasonable" rates. The Commission in this rulemaking has not determined any utility's just and reasonable rates. Further, Order No. 888 does not by its terms bar the recovery of costs that do not result from the use of Commission-required transmission access. Utilities may, as before, seek recovery of such non-open access-related costs on a case-by-case basis in individual rate proceedings. The Commission will not prejudge those issues here.

As we indicated in Order No. 888, we also are concerned that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission -- either this Commission or state commissions -- to address recovery of stranded costs.[691] We reiterate that we reserve the right to address such situations on a case-by-case basis.

---

[691]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,819; *mimeo* at pp. 536-37.

We share the concern expressed by Puget that a retail-turned-wholesale customer should not be allowed to avoid any stranded cost obligation that it may have under Order No. 888 simply by having its new supplier be the entity that requests and contracts for transmission service from the former supplying utility. We clarify that the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers under Order No. 888 applies if the transmission system of the former supplier is used to transmit the newly obtained power supplies to the departing retail customer, regardless of whether the customer or its new supplier is the actual entity that requests and contracts for the unbundled transmission service. We have revised the definition of "wholesale stranded cost" in section 35.26(b)(1)(ii) accordingly to include **[30,410]** the situation in which the retail customer subsequently becomes, either directly or through another wholesale transmission purchaser, an unbundled wholesale transmission services customer of the former supplying utility.

We clarify in response to SoCal Edison's request that our decision to be the primary forum for recovery of stranded costs from retail-turned-wholesale customers is not intended to prevent or to interfere with the authority of a state to permit any recovery from departing retail customers, such as by imposing an exit fee prior to creating the wholesale entity. As we indicated in Order No. 888, if the state has permitted any such recovery from a departing retail-turned-wholesale customer, that amount will not in fact be stranded. Accordingly, we will deduct that amount from the costs for

which the utility will be allowed to seek recovery from this Commission.[692]

We clarify in response to SoCal Edison's request that the Commission has the discretion to defer to a state stranded cost calculation methodology. However, because we recognize that state retail access plans may present questions that need to be addressed on a case-by-case basis, we will consider whether to exercise that discretion on a case-by-case basis.

7. Recovery of Stranded Costs Caused by Retail Wheeling

In Order No. 888, we concluded that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in order to reach a different generation supplier, and that utilities are entitled, from both a legal and a policy perspective, to an opportunity to recover all of their prudently incurred costs.[693] We explained that this Commission's authority to address retail stranded costs (i.e., stranded costs associated with retail wheeling customers) is based on our jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, and that the authority of state commissions to address retail stranded costs is based on their jurisdiction over local

---

[692] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,819; *mimeo* at p. 537

[693] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,824-26; *mimeo* at pp. 553-58.

distribution facilities and the service of delivering electric energy to end users. Because it is a state decision to permit or to require the retail wheeling that causes stranded costs to occur, we decided we generally will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority[694] does not have authority under state law to address stranded costs when the retail wheeling is required. In such a case, we will permit a utility to seek a customer- specific surcharge to be added to an unbundled transmission rate.

We noted that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We indicated that rates for services using facilities used in local distribution to make a retail sale are state-jurisdictional, and that states will be free to impose stranded costs caused retail wheeling on facilities or services used in local distribution. We also said that states may use their jurisdiction over local distribution facilities or services to recover so-called stranded benefits.

We stated that we believe our approach to stranded costs associated with retail wheeling customers represents an

---

[694]"State regulatory authority" has the same meaning as provided in section 3(21) of the FPA: 'State regulatory authority' has the same meaning as the term 'State commission', except that in the case of an electric utility with respect to which the Tennessee Valley Authority has ratemaking authority (as defined in section 3 of the Public Utility Regulatory Policies Act of 1978), such term means the Tennessee Valley Authority.

appropriate balance between federal and state interests that ensures that the rates for transmission in interstate commerce by public utilities (except in a narrow circumstance) will not be burdened by retail costs.

We expressed concern about the cost-shifting potential in a holding company or other multi-state situation, where denial **[30,411]** of retail stranded cost recovery by a state regulatory authority could, through operation of the reserve equalization formula in a Commission-jurisdictional intra-system agreement, inappropriately shift the disallowed costs to affiliated operating companies in other states. We said that we will deal with such situations if they arise pursuant to public utility filings under section 205 or complaints under section 206. Thus, the need to amend a jurisdictional agreement to prevent stranded costs associated with retail wheeling customers from being shifted to customers in other states will be addressed on a case-by-case basis. We encouraged the affected state commissions in such situations to seek a mutually agreeable approach to this potential problem. If such a consensus solution resulted in a filing to modify a jurisdictional agreement, we indicated that we would accord such a proposal deference, particularly if other interested parties support the filing. In the event that the state commissions and other interested parties cannot reach consensus that would prevent cost shifting, we said that the Commission would ultimately have to resolve the appropriate treatment of such stranded costs.

Rehearing Requests Opposing Any Commission Involvement in Stranded Costs Associated With Retail Wheeling Customers

A number of entities dispute the Commission's statement that both it and the states have the legal authority to address stranded costs that result from retail wheeling. Central Illinois Light contends that the Commission's claim of dual jurisdiction is inconsistent with *FPC v. Southern California Edison Company*.[695] It says that the court in that case recognized that Congress meant to draw a bright line easily ascertained between state and federal jurisdiction, making unnecessary case-by-case analysis. Central Illinois Light asserts that the Commission has stepped over the bright line into the states' exclusive jurisdiction over retail rates.

IA Com seeks rehearing of the Commission's assertion of concurrent jurisdiction with state authorities over stranded costs associated with retail wheeling customers on the ground that it is based on the Commission's erroneous assertion of jurisdiction over unbundled retail transmission.

IL Com says that regardless of whether the Commission's claim of jurisdiction over retail transmission is upheld, the Commission's ruling that there is joint jurisdiction over retail stranded costs is in error. According to IL Com, the Commission has no authority over such stranded costs. IL Com also disputes the Commission's characterization of the derivation of state authority to address such stranded costs. It says that state commission authority does not derive only from states' jurisdiction over local distribution facilities and the

---

[695]376 U.S. 205, 215-16 (1964).

service of delivering electric energy to end users. IL Com submits that state commission authority to address retail stranded costs derives from the existence of state commission jurisdiction over the facilities and costs at the time of their incurrence.

A number of entities contend that Commission jurisdiction over transmission facilities used in interstate commerce does not give it jurisdiction over stranded investment in retail generating assets.[696] Several argue that the fact that a retail wheeling customer might need transmission access from its former supplier does not change the character of the costs that are stranded. They maintain that retail stranded costs are not costs of providing unbundled transmission service, but are costs associated with providing what was formerly bundled retail service, over which the Commission has no jurisdiction.[697]

Several entities argue that it is solely the action of the state that allows a given **[30,412]** utility's retail customers to

---

[696]*E.g.*, Central Illinois Light, IN Consumer Counselor, IN Consumers, Nucor, FL Com, WI Com, VA Com, AR Com, MO/KS Com, OH Com, APPA. For example, FL Com asserts that costs for facilities that are currently under the jurisdiction of state authorities do not become the Commission's jurisdiction because retail wheeling is instituted; in most cases, the states approved both the construction and the cost recovery for these facilities under bundled rate structures. FL Com submits that the states are in a better position to judge the extent and value of assets that may become stranded as a result of retail wheeling.

[697]*E.g.*, APPA, AR Com, MO/KS Coms, OH Com.

seek alternative sources of supply; therefore, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime.[698]

A number of entities submit that the provision of FPA section 201 that federal regulation is "to extend only to those matters which are not subject to regulation by the States" bars any attempt by the Commission to displace or supplant an admittedly legitimate exercise of state authority over retail stranded costs.[699] NASUCA submits that all state commissions have the authority to establish just and reasonable rates for the retail electric utilities in their respective jurisdictions.[700] It maintains that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws; the Commission has no knowledge or expertise regarding the specific state legal frameworks in

---

[698]*E.g.*, NARUC, TAPS.

[699]*E.g.*, NASUCA, NY Com, WY Com, NARUC. The Consumer's Utility Counsel Division of the Georgia Governor's Office of Consumer Affairs filed comments on June 24, 1996, in support of NARUC's request for rehearing on the jurisdictional issues pertaining to the recovery of retail stranded costs. While answers to requests for rehearing generally are not permitted, 18 CFR §385.213(a)(2) (1996), we will depart from our general rule because of the significant nature of this proceeding and will accept these comments.

[700]According to NASUCA, whether or not that authority includes a requirement that a utility receive 100 percent return on stranded costs (or something less) is a matter to be determined by the state courts and legislatures.

which these costs were included in rates. NY Com argues that the Commission does not have jurisdiction to determine the rate treatment of costs devoted to retail service and, thus, lacks authority to allow recovery if a state decides not to do so.

VA Com argues that section 201(b)(1) of the FPA restricts the Commission's jurisdiction to wholesale sales. It says that a departing retail customer remains a retail customer, regardless of the supplier. VA Com concludes that no portion of the transaction is a wholesale sale, and that there are no wholesale costs associated with a retail wheeling transaction.[701]

A number of entities seek rehearing of the Commission's decision that it will entertain stranded cost claims when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is[702] NARUC submits that Congress did not intend the Commission to become involved in adjudicating legal questions regarding the breadth of state law authority granted state commissions by their legislatures. NARUC expresses concern that the Commission would second-guess a state cost recovery determination and promote forum shopping. Once a balance has been struck at the state level

---

[701]*See also* AR Com (one retail transaction is replaced by another retail transaction; there is no wholesale transaction and no wholesale costs over which the Commission has jurisdiction).

[702]*E.g.*, NARUC, Central Illinois Light, IN Com, American Forest & Paper, IN Consumer Counselor, IN Consumers, IL Com.

concerning the terms of restructuring, NARUC submits that it is inconceivable that the Commission would have either the desire or authority to second-guess a state's legislative and regulatory processes.

Several entities object that the Commission effectively would authorize recovery of stranded costs associated with a retail wheeling customer if a state legislature withholds from the state regulatory agency the authority to approve stranded cost recovery.[703] They submit that just because a state has not given its regulatory commission the authority to impose stranded costs in the case of retail wheeling does not confer jurisdiction on the Commission to impose such charges. They contend that the state legislature should be the final arbiter of state policy. IL Com submits that if a state legislature chooses not to give its state commission the authority to act on stranded costs, "that can be taken as a clear indication that the state's legislature most certainly does not want FERC to address them."[704] Central Illinois Light objects that the Commission has offered no reason why it will accept the decision of the **[30,413]** regulatory agency, but not that of the legislature.

AMP-Ohio and Cleveland ask the Commission to clarify that its deference to the determinations of the states is to the authority of the states as exercised through state

---

[703] *E.g.*, Central Illinois Light, IN Com, American Forest & Paper, IN Consumer Counselor, IN Consumers, IL Com. TX Com considers that it has the power to address stranded cost issues related to retail transmission service.

[704] IL Com at p. 38 (emphasis in original).

legislative bodies (and other political subdivisions with legislative authority) as well as to state regulatory bodies. They submit that if the state legislature, or a local government acting in accordance with its authority, enacts retail wheeling legislation that expressly limits the ability of its regulatory body to permit recovery of stranded costs, even barring all such recovery, the Commission should not become involved.

Several entities ask the Commission to clarify that Order No. 888 does not permit utilities to apply to the Commission for recovery of stranded costs associated with a retail wheeling customer when a state regulatory authority has "addressed" a request for the same stranded costs but has not allowed 100 percent recovery.[705] ELCON gives two hypothetical examples to which it asks the Commission to respond: one where a state regulatory authority possesses full stranded cost recovery authority but allows only 50 percent recovery; the other where the state legislature provides the state regulatory authority by statute with the power to permit recovery of up to 50 percent of identified stranded costs.

Commission Conclusion

We reaffirm our conclusion that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in interstate commerce from public utilities in order to reach a different generation supplier, but that, because it is a state decision to permit or require the retail wheeling that causes retail stranded costs to occur, we will leave it to state

---

[705] *E.g.*, ELCON, NASUCA, IL Com, NY Com.

regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required.

We will reject the requests for rehearing that oppose any Commission involvement in stranded costs associated with retail wheeling customers. We disagree with those entities that challenge our conclusion that both this Commission and the states have the legal authority to address stranded costs that result from retail wheeling (variously described by those entities as dual, concurrent, or joint jurisdiction). The Commission explained in detail in Order No. 888 the legal basis for concluding that this Commission and the state commissions each have jurisdiction over separate aspects of a retail wheeling transaction.[706] This Commission has jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities. State commissions have jurisdiction over local distribution facilities and the service of delivering electric energy to end users. Based on our respective jurisdictions over separate aspects of the retail wheeling transaction, we believe either has the authority to provide the former supplying utility with an opportunity to recover costs stranded when the departing customer uses retail transmission in interstate commerce to reach a new supplier, but that here,

---

[706] *See FERC Statutes and Regulations, Reulations Preambles January 1991-June 1996* at pp. 31,780-85; *mimeo* at pp. 427-42 and Appendix G.

unlike the retail-turned-wholesale scenario, the state commission should be the primary forum because these costs are stranded by the action of the state. We would act only if the primary forum is not available. We have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity to seek recovery of prudently incurred costs.

Several entities argue that the Commission does not have jurisdiction over stranded investment in retail generating assets, that use of Commission-jurisdictional transmission does not change the character of the costs that are stranded, that stranded costs associated with retail wheeling customers are not costs of providing unbundled transmission service, **[30, 414]** but are costs associated with providing what was formerly bundled retail service, and that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws. While we agree that stranded costs associated with retail wheeling are costs that are retail in character in the sense that they are in retail bundled rates and become stranded as a result of retail wheeling required by the state commission, we do not believe this precludes the Commission from exercising jurisdiction in the limited circumstances of the Rule.

As an initial matter, we note that there are rarely separate retail and wholesale generating facilities. Retail customers and wholesale requirements customers get energy from the same facilities, each buying a "slice of the system." Typically all generating assets go into both the retail and the wholesale rate bases for determining retail and wholesale rates. Rates are determined by allocating the total generating

costs among customer classes. The parties confuse the issue before us to the extent they suggest that state commissions, not this Commission, have "jurisdiction" over certain "costs." Neither the state commissions nor this Commission has exclusive jurisdiction over "costs." Each regulatory authority has jurisdiction to determine "rates" for services subject to its jurisdiction and, in determining rates, may take into account all of the costs incurred by the utility. Under historical cost-of-service ratemaking, each regulatory authority, in exercising its respective *ratemaking* jurisdiction, reviews the *total* costs incurred by a utility to provide service and makes its separate and independent determination of what costs may be recovered through rates within its jurisdiction.[707] Generating

---

[707]If a utility is regulated by both this Commission and a state commission, each commission, in setting cost-of- service rates within its jurisdiction, will separately and independently determine the utility's total cost of providing service (also known as the utility's total revenue requirement). This will be based on the expenses incurred in providing service and a reasonable profit on the utility's assets that are used to provide the service. The commissions may differ as to what assets are appropriately included in total rate base, what other costs are appropriately included in the total cost of service, and what rate of return should be permitted. Once each regulatory authority has determined the appropriate total revenue requirement, it then will determine what portion of that total revenue requirement should be borne by the utility's wholesale customers and what share should be borne by retail customers (also called cost allocation). Each commission may also reach different conclusions on this split as well. Thus, under historical cost-based ratemaking, regulatory authorities do not carve out so-called "wholesale costs" that only this Commission can take into account in determining rates subject to its jurisdiction or so-called "retail costs" that only a state commission can take into account in

costs continually shift between retail and wholesale rates over time.[708]

More importantly, both the state commission and this Commission have a responsibility to oversee the financial health of the utilities we regulate. Each has jurisdiction to make judgments about recovery of the costs of the assets in the utility's total rate base. Utilities are entitled to a regulatory forum that can adjudicate claims that they are or are not entitled to recovery of costs incurred regardless of the initial retail or wholesale "character" of those costs, and we believe we have the authority and obligation to fill a regulatory "gap" that could occur.[709]

---

determining rates subject to state jurisdiction. Additionally, this Commission and state commissions have the discretion to determine whether costs are appropriately recovered through a transmission, generation, or distribution component of a rate (also called functionalization of costs) within their respective jurisdictions.

[708]We reject arguments that stranded retail generation costs are not a cost of providing unbundled retail transmission. While such costs are not a cost of operating the physical transmission system, nevertheless, they are an economic cost incurred as a result of being required to provide retail transmission.

[709]This is not a regulatory "gap" in the sense that the Commission would be asserting authority over matters not within its jurisdiction. However, the Commission would be filling a regulatory "gap" to the extent that the utility normally would have the opportunity to seek approval from its state regulatory commission to recover costs in retail rates from a departing retail customer or to reallocate those costs to other retail customers. In circumstances where the utility does not have this opportunity

[30,415]

In response to the argument that it is solely the action of the state that allows a retail customer to seek alternative sources of supply and, as a result, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime, we agree. Indeed, as we indicate in Order No. 888, we decided to leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling (with a limited exception) because it is a state decision to permit or require the retail wheeling in the first instance that causes retail stranded costs to occur. Our determination, as explained above, is to fill any regulatory gap that arises as a result of interstate wheeling. We believe that it is necessary for the Commission to act as a backstop in this limited instance to ensure that costs stranded as a result of retail wheeling do not go unrecovered because the state regulatory authority lacks the authority under state law to address such costs. At the same time, as we stated in Order No. 888, we believe that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We emphasize that this Rule is not intended to preempt the exercise of any existing state authority with respect to the assessment of a stranded cost or stranded benefits charge on a retail customer that obtains retail wheeling.

---

because the state regulatory authority has no authority to address the issue, we may appropriately fill this regulatory "gap" to permit recovery from the departing customer through the retail transmission rate.

In response to arguments that the Commission's decision will result in second-guessing or interfering with a state's legislative processes and decisions, we believe these arguments are premature. As a general matter, we do not expect that our decision to be a backstop will interfere with legislative decisions that specifically address stranded cost matters and the scope of the state regulatory authority's authority in determining stranded costs. If states or parties to a retail stranded cost recovery case brought before this Commission believe that a Commission decision on the issue would interfere with state legislative decisions, they should raise their arguments, and support therefor, at that time.

We clarify that Order No. 888 does not permit utilities to seek recovery from the Commission of stranded costs associated with retail wheeling customers if a state regulatory authority with authority to address retail wheeling stranded costs has in fact addressed such costs, regardless of whether the state regulatory authority has allowed full recovery, partial recovery, or no recovery.

Rehearing Requests Supporting Broader Jurisdiction Over Stranded Costs Associated With Retail Wheeling Customers

A number of entities seek rehearing of the Commission's decision not to serve as a backstop for all stranded costs associated with retail wheeling customers. Some assert that the Commission has the legal authority to address independently stranded costs that arise from retail wheeling and that the Commission cannot lawfully abdicate or

delegate such authority to the states.[710] Coalition for Economic Competition submits that the Commission correctly concluded that it has jurisdiction over retail transmission rates, terms and conditions and the authority to address retail wheeling stranded costs. Thus, it argues that the Commission is without the power to make a "policy determination" that results in the Commission not exercising its legal authority over stranded costs associated with retail wheeling customers. It asserts that, just as the Commission recognizes that it "cannot simply turn over its jurisdiction" to the states to determine facilities subject to Commission jurisdiction,[711] the Commission cannot turn over its jurisdiction to establish stranded cost charges that it correctly determined it has the authority to establish. Coalition for Economic Competition argues that the Commission should adopt a stranded cost recovery policy similar to the policy the Commission has adopted with respect to the determination of state/federal jurisdiction, whereby the Commission would defer to state stranded cost determinations so long as they are consistent with the Commission's policy.

[30,416]

Utilities For Improved Transition argues that the Commission's authority over public utility rates for the transmission of electric power, both wholesale and retail, is plenary and exclusive. As a result, it submits that the Commission may not avoid responsibility for costs stranded

---

[710]*E.g.*, Utilities For Improved Transition, Coalition for Economic Competition.

[711]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,784; *mimeo* at p. 439.

by transmission of retail power.[712] Illinois Power contends that Congress did not authorize the Commission to reject jurisdictional rate filings whenever the Commission regards the state commissions as a more convenient or appropriate forum.

EEI and the Coalition for Economic Competition contend that virtually all retail stranded costs can only occur through the vehicle of Commission-jurisdictional transmission in interstate commerce. They submit that the Commission, having recognized the clear nexus between FERC-jurisdictional transmission and stranded costs in the retail-turned-wholesale context, cannot fail to recognize the same clear nexus in the retail wheeling context.

Utilities For Improved Transition says that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states' doing so; the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service.

Coalition for Economic Competition and Utilities For Improved Transition contend that the Commission must

---

[712]Utilities For Improved Transition argues that, based on *Consolidated Edison Company of New York, Inc.*, 15 FERC ¶61,174 at p. 61,405 (1981) and other cases, the Commission has jurisdiction over the entire delivery service (rendered on both the transmission and local distribution facilities) as a transmission transaction. Utilities For Improved Transition submits that states do not have authority over rates on local distribution facilities used to complete a transmission transaction.

consider stranded costs that arise from retail wheeling in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. Coalition for Economic Competition maintains that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (e.g., wholesale wheeling and new municipalizations) but to exclude them from other jurisdictional wheeling rates (e.g., retail wheeling, municipal annexation, and bypass).[713] Utilities For Improved Transition says that the just and reasonable standard requires the Commission to backstop the states to ensure that there is full stranded cost recovery. It objects that Order No. 888's disposition of jurisdiction creates a problem of cross-class discrimination (wholesale versus retail) and inter-class discrimination (some retail versus the remainder of the retail).

Coalition for Economic Competition further argues that the Commission's failure to address all stranded costs associated with retail wheeling customers will result in an improper taking under the Constitution.[714] It also argues that the Commission is not permitted to disregard its findings in Order No. 888 which, according to Coalition for Economic Competition, "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail

---

[713]EEI states that the Commission did not rebut EEI's argument that the Commission's failure to address all retail stranded costs was unduly discriminatory.

[714]In support of its argument, Coalition for Economic Competition cites *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 602 (1944); *Duquesne Light Company v. Barasch*, 488 U.S 299, 307-08 (1989).

wheeling, municipal annexation, and bypass stranded costs) is required.[715]

Illinois Power argues that the FPA does not authorize the Commission to discriminate among utilities based on the state of their residence, and that the Commission must allow all utilities to seek interstate rate recovery of just and reasonable retail stranded costs. Illinois Power asserts that the Rule will lead to the absurd, unduly discriminatory result that utilities located in states whose legislatures have failed to provide for stranded cost recovery will be better off than those located in states that provide for only limited stranded cost recovery. It supports use of the Commission's statutory authority to establish a uniform, national method for retail stranded cost recovery.

Coalition for Economic Competition also contends that the Commission's decision **[30,417]** to let the states deal with retail stranded costs is arbitrary and capricious because the Commission failed to consider the arguments that stranded cost opponents will make before state commissions, such as that a state lacks jurisdiction to impose stranded cost charges or that the state imposition of such charges may be preempted or found to be an undue burden on interstate commerce. It further argues that the Commission's reliance on state jurisdiction over the service of delivering electric energy to the end user does not reflect reasoned decisionmaking. It submits that the Commission has failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, in which case the state

---

[715]Coalition for Economic Competition at p. 14.

commission may have no jurisdiction over either the sale or the transmission of the energy and, accordingly, no authority to consider stranded costs.

A number of entities ask the Commission to act on requests for retail stranded cost recovery when the state commission lacks authority or has authority to order recovery, but has declined to do so or has only allowed partial recovery.[716]

Lastly, TX Com notes that section 35.26(d) (dealing with recovery of retail stranded costs) refers only to public utilities. It suggests that the omission of a reference to transmitting utilities appears to be inadvertent and should be corrected.

Commission Conclusion

The Commission will reject the requests for rehearing of our decision not to assume a backstop role for all stranded costs associated with retail wheeling customers. We explained in Order No. 888 that commenters that describe our action as an unlawful abdication or delegation of authority misconstrue the nature of our decision to leave stranded costs associated with retail wheeling customers (with a limited exception) to state regulatory authorities.[717] We have not "abdicated" or

---

[716]*E.g.*, Centerior, Southern, SoCal Edison.

[717]We also explained that the case law they cite (which they refer to again in their rehearing requests) to support the proposition that an agency is not authorized to abdicate its statutory responsibility or to delegate to parties and intervenors regulatory

"delegated" to state regulatory authorities our jurisdiction over the rates, terms, and conditions of retail transmission in interstate commerce; if retail transmission in interstate commerce by a public utility occurs, public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.[718] Instead, we have made a policy determination that the recovery of stranded costs associated with retail wheeling customers -- an issue over which either this Commission or state commissions could exercise authority by virtue of their jurisdiction over retail transmission in interstate commerce and over local distribution facilities and services, respectively -- is primarily a matter of local or state concern for which the primary forum

---

responsibilities is factually distinguishable and inapposite. *See FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,825 and note 765; *mimeo* at pp. 554-55 and note 765.

[718]The entities who argue that the Commission has abdicated or delegated its jurisdiction to the states misconstrue the Commission's jurisdiction to determine rates for unbundled transmission in interstate commerce as somehow including exclusive "jurisdiction" over "costs." However, as discussed above, neither this Commission nor the state commissions has exclusive "jurisdiction" over "costs." Rather, each has jurisdiction to determine "rates" for services subject to its jurisdiction. It is in the course of determining "rates" for unbundled transmission in interstate commerce that this Commission can take into account various costs incurred by a utility to provide jurisdictional service. A state commission can take those same costs into account in making its separate and independent determinations of what costs may be recovered through rates within its jurisdiction. See note 707, supra, and accompanying text.

should be the state commissions. However, if the state regulatory authority does not have authority under state law to be the forum to address stranded costs when the retail wheeling is required, then we will entertain requests to recover such costs. As we explain above in response to the rehearing petitioners that oppose any Commission involvement in stranded costs associated with retail wheeling customers, we have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity **[30,418]** to seek recovery of prudently incurred costs.[719]

We disagree with Coalition for Economic Competition's argument that our findings in Order No. 888 "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail wheeling and bypass stranded costs) is required, much less that the Commission has ignored the findings in Order No. 888. To the contrary, as we explain in Section IV.J.1, it is not the purpose of this Rule to allow utilities an opportunity to seek to recover "all" uneconomic costs that might be stranded when a customer leaves its utility supplier. We have fully explained our reasons for adopting an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of

[719]Based on these same considerations, we reject Coalition for Economic Competition's request that the Commission assume a backstop role for all stranded costs associated with retail wheeling customers but defer to state stranded cost determinations so long as they are consistent with the Commission's policy.

stranded cost recovery from retail customers, recognizes state commission jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures.

We disagree with those entities that contend that the Commission must consider retail stranded costs in order to satisfy our statutory obligation under the FPA to set just and reasonable rates. In determining just and reasonable rates for jurisdictional transmission service, which currently are determined on a cost basis, the Commission satisfies its statutory obligation under the FPA by allowing utilities an opportunity to recover their prudently incurred costs plus a reasonable rate of return. As we have explained above, this may include the costs of use of the physical transmission system, as well as economic costs incurred by the utility when it provides Docket Nos. RM95-8-001 -92- and RM94-7-002 transmission service (e.g., stranded costs). However, in situations in which a state regulatory authority has the authority to address recovery of retail stranded costs, there is no regulatory "gap," and there is no obligation for this Commission to provide a second opportunity for recovery.[720]

We reject arguments that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (wholesale wheeling and new municipalizations) but to

[720]If the state regulatory authority is the forum before which to seek recovery, the utility may make whatever arguments it wishes regarding the justness and reasonableness of its rates, as well as any unconstitutional taking arguments it may have, before the state forum. Further, it can pursue appeals of unfavorable decisions through the state court system.

exclude them from other jurisdictional wheeling rates (retail wheeling in interstate commerce and use of another utility's transmission tariff), and that this policy somehow makes rates discriminatory. Recovery of this type of cost through a transmission rate is obviously not the norm, but is necessitated by the need to deal with the transition costs associated with this Rule. As discussed in detail in the Rule, the Commission has carefully balanced the interests of utilities as well as customers in concluding that the opportunity for stranded cost recovery through transmission rates should be permitted in only two general circumstances: (1) in the case of wholesale stranded costs, where there is a direct nexus to Commission-required transmission access; and (2) in the case of retail stranded costs, where there otherwise would be a regulatory gap because a state regulatory authority lacks authority under state law to address stranded costs at the time that retail wheeling is required. We see nothing in the FPA that precludes us from exercising this flexibility and, indeed, the parties have not pointed to anything that, in our opinion, precludes us from exercising this discretion.

We reject the argument that virtually all stranded costs associated with retail wheeling customers can occur only through the vehicle of Commission-jurisdictional transmission in interstate commerce, and therefore, that the same nexus between FERC-jurisdictional transmission and stranded costs that exists in the retail-turned-wholesale context is present in the retail wheeling context. We also **[30,419]** disagree that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states doing so, and that the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service. The opportunity for stranded cost

recovery set forth in this Rule is based on the causal link between stranded costs and the availability and use of the Commission-required transmission tariff. It is true that in both the retail-turned-wholesale context and the retail wheeling context there is a limited nexus between stranded costs and Commission-jurisdictional access since, in both situations, the Commission has jurisdiction over the rates, terms and conditions of the transmission service and, therefore, the authority to permit stranded cost recovery through the transmission rates. However, the causal nexus to FERC-jurisdictional transmission and stranded costs in the two contexts (retail vs. retail-turned-wholesale) is different. In the retail wheeling context, there is no causal nexus between stranded costs and transmission that has been ordered by this Commission. In the retail-turned-wholesale context, in contrast, the opportunity for a utility to seek recovery of stranded costs is grounded on the existence of a direct causal nexus between stranded costs and transmission that has been *ordered by this Commission.*

We will reject the rehearing petitions that ask the Commission to act on requests for stranded cost recovery associated with retail wheeling customers not only when the state commission lacks authority, but also when the state commission has authority but either has declined to use it or has only allowed partial recovery. As explained above, our decision to entertain requests to recover stranded costs caused by retail wheeling in a limited circumstance (when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on our determination to fill any regulatory gap that arises in association with interstate transmission.

We will reject TX Com's request that the Commission clarify that section 35.26(d) (dealing with recovery of retail stranded costs), which refers only to public utilities, should also refer to transmitting utilities. The Commission's decision to act as a limited backstop in the case of stranded costs associated with retail wheeling customers is based on our jurisdiction under sections 205 and 206 of the FPA over the rates, terms, and conditions of retail transmission in interstate commerce. As a result, our ability to allow the recovery of such costs through a surcharge on a section 205 unbundled transmission rate is necessarily limited to public utilities.[721]

Rehearing Requests Opposing Commission Treatment of Stranded Costs Associated with Retail Wheeling Customers in Holding Company Intra-system Agreement Cases

A number of entities oppose the Commission's proposal to address on a case-by-case basis whether jurisdictional intra-system agreements may need to be amended in order to prevent inappropriate cost-shifting that could occur if one state disallows stranded cost recovery associated with retail wheeling customers. IN Com objects that the problem is not the actions of one state or another, but rather the terms of the intra-system agreement.

AR Com objects that Order No. 888 is factually in error because a state's treatment of retail stranded costs under

---

[721]We note that the definition of "retail stranded cost" in section 35.26(b)(5) mistakenly refers to "a public utility or transmitting utility" (emphasis added). We will revise the definition to remove the reference to "transmitting utility."

the Entergy System Agreement cannot shift costs to other jurisdictions.[722] It submits that whenever retail load changes, whether due to retail wheeling or any other factor, responsibility ratios under Entergy's reserve equalization schedule, MSS-1, will change and costs will shift irrespective of the regulator's treatment of retail stranded costs. AR Com says that MSS-1 reveals no changes in calculations due to retail treatment of stranded costs or any other retail ratemaking; only **[30,420]** "excess" capacity costs of intermediate gas- and oil-fired plant are "shifted" under the Entergy System Agreement. Although the Commission has the authority to amend intra-system agreements when wholesale cost allocations have become unjust and unreasonable, AR Com submits that the Commission does not have jurisdiction to reach to the state level and dictate what retail ratepayers should pay to shareholders. AR Com maintains that a FERC-jurisdictional intra-system agreement extends only to sales for resale (transactions among subsidiaries), and that if a holding company believes that an intra-system agreement is unduly discriminatory as a result of a state's disallowance of costs, the holding company can propose to amend it.[723]

---

[722]*See also* MO/KS Coms (the cost-shifting problem does not arise because of a particular state treatment of stranded costs; it arises because Entergy insists on recovering 100 percent of its costs even when some portion of the costs are not economical).

[723]AR Com also objects to the Commission's description of the issue as involving not only holding companies, but also other multi-state situations. AR Com says that "[t]he mere fact that a company's territory crosses state lines does not automatically mean that all assets serve all customers, or that all customers are required to bear the economic risk associated with all assets, or that assets

AR Com argues that retail stranded costs fall to state jurisdiction regardless of whether the utility is a member of an interstate holding company. AR Com says that because the costs at issue are in retail rate base, any Commission influence over their recovery could occur only through preemption, but preemption of a state disallowance from retail rate base is possible only if there is a "trapped cost." AR Com submits that a disallowance of retail rate base cost cannot result in a trapped cost because there is no inconsistency between two agencies acting within their jurisdiction; the Commission has no jurisdiction to act. AR Com maintains that, unlike the Grand Gulf situation, the Commission has not mandated any Entergy generation costs into retail rate base. It further says that different state decisions regarding recovery of retail costs are not inconsistent decisions; they represent each state applying its law to its facts. According to AR Com, decisions by states leading to less than full recovery could be deemed inconsistent decisions only if there were a federal guarantee of full cost recovery of retail costs, which there is not.

AR Com and MO/KS Coms assert that the Commission's proposal for holding company situations cannot apply to future holding companies, where there is no history of joint planning justifying cost equalization, nor can it apply to future investments. They contend that this would require an assumption that the utility subsidiaries of a registered holding company have planned, and should plan, together rather than

---

that at one time were solely state-jurisdictional can somehow, by virtue of a company's decision to expand across state lines, become FERC-jurisdictional." AR Com at p. 11.

separately (i.e., that interaffiliate transactions are always more efficient than nonaffiliate transactions), and that such assumption would be sound only if having the transaction occur between affiliates is inherently more efficient than having the transaction occur between an affiliate and a nonaffiliate.

Commission Conclusion

The comments raised for the most part are either premature or reflect a misunderstanding of the Commission's decision. Contrary to AR Com's argument, the Commission in Order No. 888 in no way asserted jurisdiction over state determinations of stranded costs associated with retail wheeling customers. We agree with AR Com that our jurisdiction extends only to sales for resale (and transmission in interstate commerce) and that a holding company can seek to amend an intra-system agreement if it believes the agreement is unduly discriminatory as a result of a state's disallowance of costs. However, a holding company also may seek to amend an agreement *before* any potential disallowances can occur, to keep cost-shifting from occurring. The fact is that intra-system agreements which involve wholesale sales among affiliate companies in different states could, through operation of their reserve equalization formulas, result in customers in one or more states having to indirectly bear stranded costs that are disallowed in another state, and the Commission has a responsibility to prevent inappropriate cost-shifting. Such determinations can be made only on a case-by-case basis. Again, as we stated in Order No. 888, we encourage affected state commissions to propose mutually agreeable solutions to this potential problem.

[30,421]

8. Evidentiary Demonstration Necessary -- Reasonable Expectation Standard

In Order No. 888, the Commission concluded that a utility seeking to recover stranded costs must demonstrate that it had a reasonable expectation of continuing to serve a customer. We stated that whether a utility had a reasonable expectation of continuing to serve a customer, and for how long, will be determined on a case-by-case basis, and will depend on all of the facts and circumstances. We also determined that the existence of a notice provision in a contract would create a rebuttable presumption that the utility had no reasonable expectation of serving the customer beyond the specified period. We said that whether or not a contract contains an "evergreen" or other automatic renewal provision will be a factor to be considered in determining whether the presumption of no reasonable expectation is rebutted in a particular case.[724]

We also said that we would apply the reasonable expectation standard to retail-turned-wholesale customers. We explained that, before the Commission will permit a utility to recover stranded costs, the utility must demonstrate that it incurred such costs based on a reasonable expectation that the retail-turned-wholesale customer would continue to receive bundled retail service. Whether the state law awards exclusive service territories and imposes a mandatory obligation to serve would be among the factors to be considered in

---

[724] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at pp. 570-72.

determining whether the reasonable expectation test is met in a particular case.[725]

We noted that Order No. 888 does not address who will bear the stranded costs caused by a departing generation customer if the Commission finds that the utility had no reasonable expectation of continuing to serve that customer. We indicated that we anticipate that, in such a case, a public utility will seek in subsequent requirements rate cases to have the costs reallocated among the remaining customers on its system. However, we stated that we were not prejudging that issue in the Rule.[726]

Rehearing Requests Opposing or Seeking Modification of the Reasonable Expectation Standard

APPA challenges the reasonable expectation standard as being too vague. It submits that the Commission has provided no guidance concerning application of the reasonable expectation standard, other than to state that it would decide the issue on a case-by-case basis. APPA objects that public utilities can exploit the uncertainty created by this standard, which will lead to costly and time-consuming litigation. IL Com supports replacing the reasonable expectation standard with a statutory, regulatory, contractual standard.

---

[725] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at p. 572. We indicated that the same procedures would apply to retail customers that obtain retail wheeling.

[726] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at pp. 572-73.

Several entities contend that there is no basis to conclude that the reasonable expectation test could ever be met. VT DPS and Valero submit that, since 1973, utilities have known that a refusal to wheel power could subject them to antitrust liability. They say that Order No. 888 ignores the breadth of NRC licensing conditions. LEPA similarly argues that the reasonable expectation standard could not be met where NRC license conditions required an explicit wheeling commitment and prohibited the utility from including in the wheeling cost any amount attributable to the loss of customers due to the wheeling. It objects that delaying a decision on stranded cost recovery in such cases holds the threat of possible stranded cost charges over the heads of bulk power purchasers and thereby chills their ability to seek competitive sellers.

TAPS asserts that there should be an irrefutable presumption that no stranded costs are due from customers with pre-existing transmission rights, including customers who were the beneficiaries of NRC license conditions.[727] TAPS submits that there can be no legitimate "reasonable expectation" that such customers **[30,422]** would continue to purchase power if the price was higher than the market price.

Occidental Chemical asks the Commission to clarify that a utility could have had no reasonable expectation of recovering stranded costs from customers who, prior to the

---

[727]AMP-Ohio submits that where transmission access and competition have existed to varying extents for decades, there should be an irrebuttable presumption of no reasonable expectation of continued service.

issuance of the NOPR, had the opportunity to switch to an alternative electric supplier or had the option of self-generating, obtaining on-site third-party generation, or municipalizing. Occidental Chemical further argues that it defies commercial expectations to allow a utility to argue that if a contract is silent on the issue of renewal, the obligation to purchase does not expire with the termination of the contract. It submits that the Commission has not shown that it has the authority to force customers to extend purchase agreements against their will in violation of accepted commercial practice.

A number of entities submit that the Commission erred in failing to treat a notice of termination provision as conclusive evidence that the utility had no reasonable expectation of continued service.[728] Several object that the Commission has failed to explain why the presence of a notice provision does not conclusively demonstrate the lack of a reasonable expectation and ipso facto terminate the obligation of the customer to purchase the product.[729] APPA objects that the Commission provided no evidence that it considered comments supporting making the presumption conclusive and that it found legally sufficient reasons to reject them.

---

[728]*E.g.*, APPA, American Forest & Paper, Central Montana EC, NRECA, TDU Systems, Oglethorpe, IMPA, VT DPS, Valero, PA Munis.

[729]*E.g.*, APPA, NRECA, TDU Systems. See also VT DPS and Valero (by signing a contract with a termination date, the utility assumed the risk that the customer will elect to leave when the contract expires).

PA Munis objects that the rebuttable presumption represents an unjustified departure from the Commission's traditional policy of enforcing the express terms of notice provisions without any inquiry into the reasonable expectations of the party, provided that the agreements were negotiated in good faith and approved by the Commission.[730] PA Munis contends that wholesale requirements customers negotiated notice provisions with the knowledge that the Commission would enforce the notice provisions according to their terms, including the specific length of the term.[731] PA Munis argues that it is arbitrary and capricious to provide utilities an opportunity to seek to amend these contracts.

Several entities submit that the rebuttable presumption invites litigation and promotes uncertainty for customers.[732] APPA objects that the Commission has failed to establish the showing that it would require to overcome the presumption.

Referring to the Commission's discussion of evergreen provisions, Central Montana EC argues that it is wrong to infer from the existence of an automatic renewal provision that the parties intended that the contract might run longer

---

[730]In support of its argument, PA Munis cites *Boston Edison Company*, 56 FPC 3414 (1976). *See also* American Forest & Paper.

[731]*Citing Kentucky Utilities Company*, 23 FERC ¶61,317 (1983); *Philadelphia Electric Company and Susquehanna Electric Company*, 65 FERC ¶61,303 (1993).

[732]*E.g.*, NRECA, IMPA, PA Munis.

than its initial term. Central Montana EC asserts that the presence of an evergreen provision infers simply that the parties agreed upon a mechanism to avoid the renegotiation of a power supply contract if, at the conclusion of its initial term, the parties were satisfied with the contract. It maintains that the parties' obligations are defined by the term and termination provisions of wholesale power contracts, and that the presence of a mechanism to avoid contract renegotiation does not alter those termination rights.

Commission Conclusion

We will reject the requests for rehearing of our decision to adopt a reasonable expectation standard to be applied on a case- by-case basis and to treat a notice provision in a contract as a rebuttable, not a conclusive, presumption of no reasonable expectation. Contrary to the claims of some entities, the Commission has explained the basis for its finding that utilities may have had an implicit obligation to serve their wholesale requirements customers and, therefore, that a utility should be given an opportunity to demonstrate that it incurred costs to provide **[30,423]** service to a customer and that it had a reasonable expectation that it would continue to serve the customer beyond the contract termination date. The same factors that some petitioners contend establish the absence of a reasonable expectation of continued service may be offered as evidence to be considered in determining whether the reasonable expectation test is met in a particular case.

We believe that our decision to treat a notice of termination provision in a contract as creating a rebuttable presumption that the utility had no reasonable expectation of

serving the customer beyond the period provided for in the notice provision is a reasonable one. It places evidentiary significance on the fact that a contract contains a notice of termination provision. Moreover, while it gives the utility an opportunity, based on the facts and circumstances of a particular case, to rebut the presumption of no reasonable expectation, it firmly places the burden of establishing reasonable expectation on the utility. Although some entities support treating notice provisions as a conclusive presumption of no reasonable expectation, as discussed below, we decline to adopt such an inflexible approach. Nevertheless, as we indicated in Order No. 888, when a utility is seeking a contract amendment to permit stranded cost recovery based on expectations beyond the stated term of the contract, we believe that the utility has a heavy burden in demonstrating that the contract ought to be modified.[733]

Contrary to the position of PA Munis, the rebuttable presumption is fully consistent with the Commission's past treatment of notice provisions. For example, the Kentucky Utilities Company case cited by PA Munis supports the proposition that, until a customer exercises a notice of termination provision, the utility is under an implicit obligation to continue to serve and plan for the future needs of the customer.[734] Thus, the presence of a notice of

---

[733] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,665, 31,813-14; *mimeo* at p. 87, 522.

[734] *See Kentucky Utilities Company*, 23 FERC at pp. 61,679-80 ("Once it receives an effective notice of cancellation, Kentucky can stop planning for the future needs of that customer. . . . To be

termination provision in a contract (particularly one not yet exercised by the customer), in and of itself, may not necessarily support the conclusion that the utility could never prove that it reasonably expected to continue serving the customer beyond the notice period.[735]

In response to APPA's objection that the Commission has failed to establish the showing that it would require to overcome the presumption, we note that the Commission cannot establish such a showing upfront because whether there is sufficient evidence to rebut the presumption of no reasonable expectation will depend on the facts of each case.

We appreciate the concerns expressed by some entities that the rebuttable presumption may increase the customer's uncertainty by inviting litigation. We have carefully weighed the pros and cons of treating a notice provision as a rebuttable presumption of no reasonable expectation versus the pros and cons of treating it as a conclusive presumption of no reasonable expectation. It is true, as some entities assert, that the rebuttable presumption approach presents the potential for litigation between the parties as to whether, in a particular case, the utility can rebut the presumption. The alternative

---

effective a notice of cancellation must contain a specification of the source of supply, the date on which the source of supply will be available, and an affidavit from the supplier that it will supply the customer on the date the contract ends.").

[735] *See Potomac Electric Power Company*, 43 FERC ¶61,189 (1988) (suspending a notice of termination for five months due to questions about the impact of the proposed cancellation on service reliability).

would be to treat all contracts with notice of termination provisions as conclusive evidence that the utility could have had no reasonable expectation that it would continue to serve the customer beyond the specified notice period. While the latter approach presumably would reduce the number of cases in which the issue of a utility's reasonable expectation would have to be litigated, it would do so only by prohibiting a utility from ever demonstrating that, notwithstanding the existence of a notice provision, based on the facts of a particular case, the utility reasonably expected to continue serving the customer. While we do not prejudge the likelihood of a utility being able to rebut the presumption in a particular case, we believe that **[30,424]** it would not be in the public interest for the Commission to absolutely preclude a utility from being able to make such a showing. On this basis, we conclude that treating a notice provision as a rebuttable, rather than a conclusive, presumption that the utility did not have a reasonable expectation of continuing service to the customer is, on balance, the fairer and more equitable approach.

Central Montana EC asserts that it is wrong to infer from the existence of an automatic renewal provision that the parties intended that the contract might run longer than its initial term. However, our statement in Order No. 888 that the existence of an automatic renewal provision will be a factor to be considered in determining whether the presumption of no reasonable expectation is rebutted in a particular case makes no such inference. Whether the utility can rebut the presumption will depend on the facts of each case.

* * * * *

[pp. 30,503-30,543]

[30,503]

Appendix B--Pro Forma Open Access Transmission Tariff

Table of Contents

I. Common Service Provisions

1 *Definitions*

1.1 Ancillary Services
1.2 Annual Transmission Costs
1.3 Application
1.4 Commission
1.5 Completed Application
1.6 Control Area
1.7 Curtailment
1.8 Delivering Party
1.9 Designated Agent
1.10 Direct Assignment Facilities
1.11 Eligible Customer
1.12 Facilities Study
1.13 Firm Point-To-Point Transmission Service
1.14 Good Utility Practice
1.15 Interruption
1.16 Load Ratio Share
1.17 Load Shedding
1.18 Long-Term Firm Point-To-Point Transmission Service
1.19 Native Load Customers
1.20 Network Customer
1.21 Network Integration Transmission Service
1.22 Network Load
1.23 Network Operating Agreement

1.24 Network Operating Committee
[30,504]
1.25 Network Resource
1.26 Network Upgrades
1.27 Non-Firm Point-To-Point Transmission Service
1.28 Open Access Same-Time Information System (OASIS)
1.29 Part I
1.30 Part II
1.31 Part III
1.32 Parties
1.33 Point(s) of Delivery
1.34 Point(s) of Receipt
1.35 Point-To-Point Transmission Service
1.36 Power Purchaser
1.37 Receiving Party
1.38 Regional Transmission Group (RTG)
1.39 Reserved Capacity
1.40 Service Agreement
1.41 Service Commencement Date
1.42 Short-Term Firm Point-To-Point Transmission Service
1.43 System Impact Study
1.44 Third-Party Sale
1.45 Transmission Customer
1.46 Transmission Provider
1.47 Transmission Provider's Monthly Transmission System Peak
1.48 Transmission Service
1.49 Transmission System
2 *Initial Allocation and Renewal Procedures*

2.1 Initial Allocation of Available Transmission Capability
2.2 Reservation Priority For Existing Firm Service Customers
3 *Ancillary Services*
3.1 Scheduling, System Control and Dispatch Service 23
3.2 Reactive Supply and Voltage Control from Generation Sources Service
3.3 Regulation and Frequency Response Service
3.4 Energy Imbalance Service
3.5 Operating Reserve - Spinning Reserve Service
3.6 Operating Reserve - Supplemental Reserve Service
4 *Open Access Same-Time Information System (OASIS)*
5 *Local Furnishing Bonds*
5.1 Transmission Providers That Own Facilities Financed by Local Furnishing Bonds
5.2 Alternative Procedures for Requesting Transmission Service
6 *Reciprocity*
***7 Billing* and Payment**
7.1 Billing Procedure
7.2 Interest on Unpaid Balances
7.3 Customer Default
8 *Accounting for the Transmission Provider's Use of the Tariff*
8.1 Transmission Revenues
8.2 Study Costs and Revenues

9 ***Regulatory Filings***
10 ***Force Majeure and Indemnification***
10.1 Force Majeure
10.2 Indemnification
11 ***Creditworthiness***
12 ***Dispute Resolution Procedures***
12.1 Internal Dispute Resolution Procedures
12.2 External Arbitration Procedures
12.3 Arbitration Decisions
12.4 Costs
12.5 Rights Under The Federal Power Act
II. POINT-TO-POINT TRANSMISSION SERVICE
Preamble
13 ***Nature of Firm Point-To-Point Transmission Service***
13.1 Term
13.2 Reservation Priority
13.3 Use of Firm Transmission Service by the Transmission Provider
13.4 Service Agreements
13.5 Transmission Customer Obligations for Facility Additions or Redispatch Costs
13.6 Curtailment of Firm Transmission Service
13.7 Classification of Firm Transmission Service
13.8 Scheduling of Firm Point-To-Point Transmission Service
[30,505]
14 ***Nature of Non-Firm Point-To-Point Transmission Service***
14.1 Term
14.2 Reservation Priority

14.3 Use of Non-Firm Point-To-Point Transmission Service by the Transmission Provider
14.4 Service Agreements
14.5 Classification of Non-Firm Point-To-Point Transmission Service
14.6 Scheduling of Non-Firm Point-To-Point Transmission Service
14.7 Curtailment or Interruption of Service
15 ***Service Availability***
15.1 General Conditions
15.2 Determination of Available Transmission Capability
15.3 Initiating Service in the Absence of an Executed Service Agreement
15.4 Obligation to Provide Transmission Service that Requires Expansion or Modification of the Transmission System
15.5 Deferral of Service
15.6 Other Transmission Service Schedules
15.7 Real Power Losses
16 ***Transmission Customer Responsibilities***
16.1 Conditions Required of Transmission Customers
16.2 Transmission Customer Responsibility for Third- Party Arrangements
17 ***Procedures for Arranging Firm Point-To-Point Transmission Service***
17.1 Application
17.2 Completed Application
17.3 Deposit
17.4 Notice of Deficient Application
17.5 Response to a Completed Application
17.6 Execution of Service Agreement

17.7 Extensions for Commencement of Service

18 ***Procedures for Arranging Non-Firm Point-To-Point Transmission Service***

18.1 Application

18.2 Completed Application

18.3 Reservation of Non-Firm Point-To-Point Transmission Service

18.4 Determination of Available Transmission Capability

19 ***Additional Study Procedures For Firm Point-To-Point Transmission Service Requests***

19.1 Notice of Need for System Impact Study

19.2 System Impact Study Agreement and Cost Reimbursement

19.3 System Impact Study Procedures

19.4 Facilities Study Procedures

19.5 Facilities Study Modifications

19.6 Due Diligence in Completing New Facilities

19.7 Partial Interim Service

19.8 Expedited Procedures for New Facilities

20 ***Procedures if The Transmission Provider is Unable to Complete New Transmission Facilities for Firm Point-To-Point Transmission Service***

20.1 Delays in Construction of New Facilities

20.2 Alternatives to the Original Facility Additions

20.3 Refund Obligation for Unfinished Facility Additions

21 ***Provisions Relating to Transmission Construction and Services on the Systems of Other Utilities***

21.1 Responsibility for Third-Party System Additions

21.2 Coordination of Third-Party System Additions

22 ***Changes in Service Specifications***

22.1 Modifications On a Non-Firm Basis

22.2 Modification On a Firm Basis

23 ***Sale or Assignment of Transmission Service***

23.1 Procedures for Assignment or Transfer of Service

23.2 Limitations on Assignment or Transfer of Service

23.3 Information on Assignment or Transfer of Service

[30506]

24 ***Metering and Power Factor Correction at Receipt and Delivery Points(s)***

24.1 Transmission Customer Obligations

24.2 Transmission Provider Access to Metering Data

24.3 Power Factor

25 ***Compensation for Transmission Service***

26 ***Stranded Cost Recovery***

27 ***Compensation for New Facilities and Redispatch Costs***

III. NETWORK INTEGRATION TRANSMISSION SERVICE Preamble

28 ***Nature of Network Integration Transmission Service***

28.1 Scope of Service

28.2 Transmission Provider Responsibilities

28.3 Network Integration Transmission Service

28.4 Secondary Service

28.5 Real Power Losses

28.6 Restrictions on Use of Service

29 ***Initiating Service***

29.1 Condition Precedent for Receiving Service

29.2 Application Procedures

29.3 Technical Arrangements to be Completed Prior to Commencement of Service

29.4 Network Customer Facilities

29.5 Filing of Service Agreement

30 ***Network Resources***

30.1 Designation of Network Resources

30.2 Designation of New Network Resources

30.3 Termination of Network Resources

30.4 Operation of Network Resources

30.5 Network Customer Redispatch Obligation

30.6 Transmission Arrangements for Network Resources Not Physically Interconnected With The Transmission Provider

30.7 Limitation on Designation of Network Resources

30.8 Use of Interface Capacity by the Network Customer

30.9 Network Customer Owned Transmission Facilities

31 ***Designation of Network Load***

31.1 Network Load

31.2 New Network Loads Connected With the Transmission Provider

31.3 Network Load Not Physically Interconnected with the Transmission Provider

31.4 New Interconnection Points

31.5 Changes in Service Requests

31.6 Annual Load and Resource Information Updates

32 ***Additional Study Procedures For Network Integration Transmission Service Requests***

32.1 Notice of Need for System Impact Study

32.2 System Impact Study Agreement and Cost Reimbursement

32.3 System Impact Study Procedures

32.4 Facilities Study Procedures

33 ***Load Shedding and Curtailments***

33.1 Procedures

33.2 Transmission Constraints

33.3 Cost Responsibility for Relieving Transmission Constraints

33.4 Curtailments of Scheduled Deliveries

33.5 Allocation of Curtailments

33.6 Load Shedding

33.7 System Reliability

34 ***Rates and Charges***

34.1 Monthly Demand Charge

34.2 Determination of Network Customer's Monthly Network Load

34.3 Determination of Transmission Provider's Monthly Transmission System Load

34.4 Redispatch Charge

34.5 Stranded Cost Recovery

35 ***Operating Arrangements***

35.1 Operation under The Network Operating Agreement

35.2 Network Operating Agreement

35.3 Network Operating Committee

[30,507]

Schedule 1

Scheduling, System Control and Dispatch Service

Schedule 2
Reactive Supply and Voltage Control from Generation Sources Service
Schedule 3
Regulation and Frequency Response Service Schedule
Schedule 4
Energy Imbalance Service
Schedule 5
Operating Reserve - Spinning Reserve Service
Schedule 6
Operating Reserve - Supplemental Reserve Service
Schedule 7
Long-Term Firm and Short-Term Firm Point-To-Point Transmission Service
Schedule 8
Non-Firm Point-To-Point Transmission Service
Attachment A
Form Of Service Agreement For Firm Point-To-Point Transmission Service
Attachment B
Form Of Service Agreement For Non-Firm Point-To-Point Transmission Service
Attachment C
Methodology To Assess Available Transmission Capability
Attachment D
Methodology for Completing a System Impact Study
Attachment E
Index Of Point-To-Point Transmission Service Customers
Attachment F
Service Agreement For Network Integration Transmission Service

Attachment G
Network Operating Agreement
Attachment H
Annual Transmission Revenue Requirement For Network Integration Transmission Service
Attachment I
Index Of Network Integration Transmission Service Customers

I. Common Service Provisions

1 Definitions

1.1 Ancillary Services: Those services that are necessary to support the transmission of capacity and energy from resources to loads while maintaining reliable operation of the Transmission Provider's Transmission System in accordance with Good Utility Practice.

1.2 Annual Transmission Costs: The total annual cost of the Transmission System for purposes of Network Integration Transmission Service shall be the amount specified in Attachment H until amended by the Transmission Provider or modified by the Commission.

1.3 Application: A request by an Eligible Customer for transmission service pursuant to the provisions of the Tariff.

1.4 Commission: The Federal Energy Regulatory Commission.

1.5 Completed Application: An Application that satisfies all of the information and other requirements of the Tariff, including any required deposit.

1.6 Control Area: An electric power system or combination of electric power systems to which a common automatic generation control scheme is applied in order to:

(1) match, at all times, the power output of the generators within the electric power system(s) and capacity and energy purchased from entities (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 10 outside the electric power system(s), with the load within the electric power system(s);

(2) maintain scheduled interchange with other Control Areas, within the limits of Good Utility Practice;

(3) maintain the frequency of the electric power system(s) within reasonable limits in accordance with Good Utility Practice; and

(4) provide sufficient generating capacity to maintain operating reserves in accordance with Good Utility Practice.

1.7 Curtailment: A reduction in firm or non-firm transmission service in response to a transmission capacity **[30,508]** shortage as a result of system reliability conditions.

1.8 Delivering Party: The entity supplying capacity and energy to be transmitted at Point(s) of Receipt.

1.9 Designated Agent: Any entity that performs actions or functions on behalf of the Transmission Provider, an Eligible Customer, or the Transmission Customer required under the Tariff.

1.10 Direct Assignment Facilities: Facilities or portions of facilities that are constructed by the Transmission Provider for the sole use/benefit of a particular Transmission Customer requesting service under the Tariff. Direct Assignment Facilities shall be specified in the Service Agreement that governs service to the Transmission Customer and shall be subject to Commission approval.

1.11 Eligible Customer: (i) Any electric utility (including the Transmission Provider and any power marketer), Federal power marketing agency, or any person generating electric energy for sale for resale is an Eligible Customer under the Tariff. Electric energy sold or produced by such entity may be electric energy produced in the United States, Canada or Mexico. However, with respect to transmission service that the Commission is prohibited from ordering by Section 212(h) of the Federal Power Act, such entity is eligible only if the service is provided pursuant to a state requirement that the Transmission Provider offer the unbundled transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider. (ii) Any retail customer taking unbundled transmission service pursuant to a state requirement that the Transmission Provider offer the transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider, is an Eligible Customer under the Tariff.

1.12 Facilities Study: An engineering study conducted by the Transmission Provider to determine the required modifications to the Transmission Provider's Transmission System, including the cost and scheduled completion date for such modifications, that will be required to provide the requested transmission service.

1.13 Firm Point-To-Point Transmission Service: Transmission Service under this Tariff that is reserved and/or scheduled between specified Points of Receipt and Delivery pursuant to Part II of this Tariff.

1.14 Good Utility Practice: Any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry during the relevant time period, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at a reasonable cost consistent with good business practices, reliability, safety and expedition. Good Utility Practice is not intended to be limited to the optimum practice, method, or act to the exclusion of all others, but rather to be acceptable practices, methods, or acts generally accepted in the region.

1.15 Interruption: A reduction in non-firm transmission service due to economic reasons pursuant to Section 14.7.

1.16 Load Ratio Share: Ratio of a Transmission Customer's Network Load to the Transmission Provider's total load computed in accordance with Sections 34.2 and 34.3 of the Network Integration Transmission Service under

Part III the Tariff and calculated on a rolling twelve month basis.

1.17 Load Shedding: The systematic reduction of system demand by temporarily decreasing load in response to transmission system or area capacity shortages, system instability, or voltage control considerations under Part III of the Tariff.

1.18 Long-Term Firm Point-To-Point Transmission Service: Firm Point-To-Point Transmission Service under Part II of the Tariff with a term of one year or more.

1.19 Native Load Customers: The wholesale and retail power customers of the Transmission Provider on whose behalf the Transmission Provider, by statute, franchise, regulatory requirement, or contract, has undertaken an obligation to construct and operate the Transmission Provider's system to meet the reliable electric needs of such customers.

[30,509]

1.20 Network Customer: An entity receiving transmission service pursuant to the terms of the Transmission Provider's Network Integration Transmission Service under Part III of the Tariff.

1.21 Network Integration Transmission Service: The transmission service provided under Part III of the Tariff.

1.22 Network Load: The load that a Network Customer designates for Network Integration Transmission Service under Part III of the Tariff. The Network Customer's

Network Load shall include all load served by the output of any Network Resources designated by the Network Customer. A Network Customer may elect to designate less than its total load as Network Load but may not designate only part of the load at a discrete Point of Delivery. Where a Eligible Customer has elected not to designate a particular load at discrete points of delivery as Network Load, the Eligible Customer is responsible for making separate arrangements under Part II of the Tariff for any Point-To-Point Transmission Service that may be necessary for such non-designated load.

1.23 Network Operating Agreement: An executed agreement that contains the terms and conditions under which the Network Customer shall operate its facilities and the technical and operational matters associated with the implementation of Network Integration Transmission Service under Part III of the Tariff.

1.24 Network Operating Committee: A group made up of representatives from the Network Customer(s) and the Transmission Provider established to coordinate operating criteria and other technical considerations required for implementation of Network Integration Transmission Service under Part III of this Tariff.

1.25 Network Resource: Any designated generating resource owned, purchased or leased by a Network Customer under the Network Integration Transmission Service Tariff. Network Resources do not include any resource, or any portion thereof, that is committed for sale to third parties or otherwise cannot be called upon to meet the Network Customer's Network Load on a non-interruptible basis.

1.26 Network Upgrades: Modifications or additions to transmission-related facilities that are integrated with and support the Transmission Provider's overall Transmission System for the general benefit of all users of such Transmission System.

1.27 Non-Firm Point-To-Point Transmission Service: Point-To-Point Transmission Service under the Tariff that is reserved and scheduled on an as-available basis and is subject to Curtailment or Interruption as set forth in Section 14.7 under Part II of this Tariff. Non-Firm Point-To-Point Transmission Service is available on a stand-alone basis for periods ranging from one hour to one month.

1.28 Open Access Same-Time Information System (OASIS): The information system and standards of conduct contained in Part 37 of the Commission's regulations and all additional requirements implemented by subsequent Commission orders dealing with OASIS.

1.29 Part I: Tariff Definitions and Common Service Provisions contained in Sections 2 through 12.

1.30 Part II: Tariff Sections 13 through 27 pertaining to Point-To-Point Transmission Service in conjunction with the applicable Common Service Provisions of Part I and appropriate Schedules and Attachments.

1.31 Part III: Tariff Sections 28 through 35 pertaining to Network Integration Transmission Service in conjunction with the applicable Common Service Provisions of Part I and appropriate Schedules and Attachments.

1.32 Parties: The Transmission Provider and the Transmission Customer receiving service under the Tariff.

1.33 Point(s) of Delivery: Point(s) on the Transmission Provider's Transmission System where capacity and energy transmitted by the Transmission Provider will be made available to the Receiving Party under Part II of the Tariff. The Point(s) of Delivery shall be (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 17 specified in the Service Agreement for Long-Term Firm Point-To-Point Transmission Service.

1.34 Point(s) of Receipt: Point(s) of interconnection on the Transmission **[30,510]** Provider's Transmission System where capacity and energy will be made available to the Transmission Provider by the Delivering Party under Part II of the Tariff. The Point(s) of Receipt shall be specified in the Service Agreement for Long-Term Firm Point-To-Point Transmission Service.

1.35 Point-To-Point Transmission Service: The reservation and transmission of capacity and energy on either a firm or non-firm basis from the Point(s) of Receipt to the Point(s) of Delivery under Part II of the Tariff.

1.36 Power Purchaser: The entity that is purchasing the capacity and energy to be transmitted under the Tariff.

1.37 Receiving Party: The entity receiving the capacity and energy transmitted by the Transmission Provider to Point(s) of Delivery.

1.38 Regional Transmission Group (RTG): A voluntary organization of transmission owners, transmission users and other entities approved by the Commission to efficiently coordinate transmission planning (and expansion), operation and use on a regional (and interregional) basis.

1.39 Reserved Capacity: The maximum amount of capacity and energy that the Transmission Provider agrees to transmit for the Transmission Customer over the Transmission Provider's Transmission System between the Point(s) of Receipt and the Point(s) of Delivery under Part II of the Tariff. Reserved Capacity shall be expressed in terms of whole megawatts on a sixty (60) minute interval (commencing on the clock hour) basis.

1.40 Service Agreement: The initial agreement and any amendments or supplements thereto entered into by the Transmission Customer and the Transmission Provider for service under the Tariff.

1.41 Service Commencement Date: The date the Transmission Provider begins to provide service pursuant to the terms of an executed Service Agreement, or the date the Transmission Provider begins to provide service in accordance with Section 15.3 or Section 29.1 under the Tariff.

1.42 Short-Term Firm Point-To-Point Transmission Service: Firm Point-To-Point Transmission Service under Part II of the Tariff with a term of less than one year.

1.43 System Impact Study: An assessment by the Transmission Provider of (i) the adequacy of the Transmission

System to accommodate a request for either Firm Point-To-Point Transmission Service or Network Integration

Transmission Service and (ii) whether any additional costs may be incurred in order to provide transmission service.

1.44 Third-Party Sale: Any sale for resale in interstate commerce to a Power Purchaser that is not designated as part of Network Load under the Network Integration Transmission Service.

1.45 Transmission Customer: Any Eligible Customer (or its Designated Agent) that (i) executes a Service Agreement, or (ii) requests in writing that the Transmission Provider file with the Commission, a proposed unexecuted Service Agreement to receive transmission service under Part II of the Tariff. This term is used in the Part I Common Service Provisions to include customers receiving transmission service under Part II and Part III of this Tariff.

1.46 Transmission Provider: The public utility (or its Designated Agent) that owns, controls, or operates facilities used for the transmission of electric energy in interstate commerce and provides transmission service under the Tariff.

1.47 Transmission Provider's Monthly Transmission System Peak: The maximum firm usage of the Transmission Provider's Transmission System in a calendar month.

1.48 Transmission Service: Point-To-Point Transmission Service provided under Part II of the Tariff on a firm and non-firm basis.

1.49 Transmission System: The facilities owned, controlled or operated by the Transmission Provider that are used to provide transmission service under Part II and Part III of the Tariff.

2 *Initial Allocation and Renewal Procedures*

2.1 Initial Allocation of Available Transmission Capability: For purposes of determining whether existing **[30,511]** capability on the Transmission Provider's Transmission System is adequate to accommodate a request for firm service under this Tariff, all Completed Applications for new firm transmission service received during the initial sixty (60) day period commencing with the effective date of the Tariff will be deemed to have been filed simultaneously. A lottery system conducted by an independent party shall be used to assign priorities for Completed Applications filed simultaneously. All Completed Applications for firm transmission service received after the initial sixty (60) day period shall be assigned a priority pursuant to Section 13.2.

2.2 Reservation Priority For Existing Firm Service Customers: Existing firm service customers (wholesale requirements and transmission-only, with a contract term of one-year or more), have the right to continue to take transmission service from the Transmission Provider when the contract expires, rolls over or is renewed. This transmission reservation priority is independent of whether the existing customer continues to purchase capacity and energy from the Transmission Provider or elects to purchase capacity and energy from another supplier. If at the end of the contract term, the Transmission Provider's Transmission System cannot accommodate all of the requests for transmission

service the existing firm service customer must agree to accept a contract term at least equal to a competing request by any new Eligible Customer and to pay the current just and reasonable rate, as approved by the Commission, for such service. This transmission reservation priority for existing firm service customers is an ongoing right that may be exercised at the end of all firm contract terms of one-year or longer.

3 *Ancillary Services*

Ancillary Services are needed with transmission service to maintain reliability within and among the Control Areas affected by the transmission service. The Transmission Provider is required to provide (or offer to arrange with the local Control Area operator as discussed below), and the Transmission Customer is required to purchase, the following Ancillary Services (i) Scheduling, System Control and Dispatch, and (ii) Reactive Supply and Voltage Control from Generation Sources.

The Transmission Provider is required to offer to provide (or offer to arrange with the local Control Area operator as discussed below) the following Ancillary Services only to the Transmission Customer serving load within the Transmission Provider's Control Area (i) Regulation and Frequency Response, (ii) Energy Imbalance, (iii) Operating Reserve - Spinning, and (iv) Operating Reserve - Supplemental. The Transmission Customer serving load within the Transmission Provider's Control Area is required to acquire these Ancillary Services, whether from the Transmission Provider, from a third party, or by self-supply. The Transmission Customer may not decline the Transmission

Provider's offer of Ancillary Services unless it demonstrates that it has acquired the Ancillary Services from another source. The Transmission Customer must list in its Application which Ancillary Services it will purchase from the Transmission Provider.

If the Transmission Provider is a public utility providing transmission service but is not a Control Area operator, it may be unable to provide some or all of the Ancillary Services. In this case, the Transmission Provider can fulfill its obligation to provide Ancillary Services by acting as the Transmission Customer's agent to secure these Ancillary Services from the Control Area operator. The Transmission Customer may elect to (i) have the Transmission Provider act as its agent, (ii) secure the Ancillary Services directly from the Control Area operator, or (iii) secure the Ancillary Services (discussed in Schedules 3, 4, 5 and 6) from a third party or by self-supply when technically feasible.

The Transmission Provider shall specify the rate treatment and all related terms and conditions in the event of an unauthorized use of Ancillary Services by the Transmission Customer.

The specific Ancillary Services, prices and/or compensation methods are described on the Schedules that are attached to and made a part of the Tariff. Three principal requirements apply to discounts for Ancillary Services provided by the Transmission Provider in conjunction with its provision of transmission service **[30,512]** as follows: (1) any offer of a discount made by the Transmission Provider must be announced to all Eligible Customers solely by posting on the OASIS, (2) any customer-initiated requests for discounts

(including requests for use by one's wholesale merchant or an affiliate's use) must occur solely by posting on the OASIS, and (3) once a discount is negotiated, details must be immediately posted on the OASIS. A discount agreed upon for an Ancillary Service must be offered for the same period to all Eligible Customers on the Transmission Provider's system. Sections 3.1 through 3.6 below list the six Ancillary Services.

3.1 Scheduling, System Control and Dispatch Service: The rates and/or methodology are described in Schedule 1.

3.2 Reactive Supply and Voltage Control from Generation Sources Service: The rates and/or methodology are described in Schedule 2.

3.3 Regulation and Frequency Response Service: Where applicable the rates and/or methodology are described in Schedule 3.

3.4 Energy Imbalance Service: Where applicable the rates and/or methodology are described in Schedule 4.

3.5 Operating Reserve - Spinning Reserve Service: Where applicable the rates and/or methodology are described in Schedule 5.

3.6 Operating Reserve - Supplemental Reserve Service: Where applicable the rates and/or methodology are described in Schedule 6.

4 Open Access Same-Time Information System (OASIS)

Terms and conditions regarding Open Access Same-Time Information System and standards of conduct are set forth in 18 CFR §37 of the Commission's regulations (Open Access Same-Time Information System and Standards of Conduct for Public Utilities). In the event available transmission capability as posted on the OASIS is insufficient to accommodate a request for firm transmission service, additional studies may be required as provided by this Tariff pursuant to Sections 19 and 32.

5 Local Furnishing Bonds

5.1 Transmission Providers That Own Facilities Financed by Local Furnishing Bonds: This provision is applicable only to Transmission Providers that have financed facilities for the local furnishing of electric energy with tax-exempt bonds, as described in Section 142(f) of the Internal Revenue Code ("local furnishing bonds"). Notwithstanding any other provision of this Tariff, the Transmission Provider shall not be required to provide transmission service to any Eligible Customer pursuant to this Tariff if the provision of such transmission service would jeopardize the tax- exempt status of any local furnishing bond(s) used to finance the Transmission Provider's facilities that would be used in providing such transmission service.

5.2 Alternative Procedures for Requesting Transmission Service:

(i) If the Transmission Provider determines that the provision of transmission service requested by an Eligible

Customer would jeopardize the tax-exempt status of any local furnishing bond(s) used to finance its facilities that would be used in providing such transmission service, it shall (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 26 advise the Eligible Customer within thirty (30) days of receipt of the Completed Application.

(ii) If the Eligible Customer thereafter renews its request for the same transmission service referred to in (i) by tendering an application under Section 211 of the Federal Power Act, the Transmission Provider, within ten (10) days of receiving a copy of the Section 211 application, will waive its rights to a request for service under Section 213(a) of the Federal Power Act and to the issuance of a proposed order under Section 212(c) of the Federal Power Act. The Commission, upon receipt of the Transmission Provider's waiver of its rights to a request for service under Section 213(a) of the Federal Power Act and to the issuance of a proposed order under Section 212(c) of the Federal Power Act, shall issue an order under Section 211 of the Federal Power Act. Upon issuance of the order under Section 211 of the Federal Power Act, the Transmission Provider shall be required to provide the requested transmission service in accordance with the terms and conditions of this Tariff.

[30,513]
6 *Reciprocity*

A Transmission Customer receiving transmission service under this Tariff agrees to provide comparable transmission service that it is capable of providing to the Transmission Provider on similar terms and conditions over facilities used for the transmission of electric energy owned,

controlled or operated by the Transmission Customer and over facilities used for the transmission of electric energy owned, controlled or operated by the Transmission Customer's corporate affiliates. A Transmission Customer that is a member of a power pool or Regional Transmission Group also agrees to provide comparable transmission service to the members of such power pool and Regional Transmission Group on similar terms and conditions over facilities used for the transmission of electric energy owned, controlled or operated by the Transmission Customer and over facilities used for the transmission of electric energy owned, controlled or operated by the Transmission Customer's corporate affiliates.

This reciprocity requirement applies not only to the Transmission Customer that obtains transmission service under the Tariff, but also to all parties to a transaction that involves the use of transmission service under the Tariff, including the power seller, buyer and any intermediary, such as a power marketer. This reciprocity requirement also applies to any Eligible Customer that owns, controls or operates transmission facilities that uses an intermediary, such as a power marketer, (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 28 to request transmission service under the Tariff. If the Transmission Customer does not own, control or operate transmission facilities, it must include in its Application a sworn statement of one of its duly authorized officers or other representatives that the purpose of its Application is not to assist an Eligible Customer to avoid the requirements of this provision.

7 *Billing and Payment*

7.1 Billing Procedure: Within a reasonable time after the first day of each month, the Transmission Provider shall submit an invoice to the Transmission Customer for the charges for all services furnished under the Tariff during the preceding month. The invoice shall be paid by the Transmission Customer within twenty (20) days of receipt. All payments shall be made in immediately available funds payable to the Transmission Provider, or by wire transfer to a bank named by the Transmission Provider.

7.2 Interest on Unpaid Balances: Interest on any unpaid amounts (including amounts placed in escrow) shall be calculated in accordance with the methodology specified for interest on refunds in the Commission's regulations at 18 C.F.R §35.19a(a)(2)(iii). Interest on delinquent amounts shall be calculated from the due date of the bill to the date of payment. When payments are made by mail, bills shall be considered as having been paid on the date of receipt by the Transmission Provider.

7.3 Customer Default: In the event the Transmission Customer fails, for any reason other than a billing dispute as described below, to make payment to the Transmission Provider on or before the due date as described above, and such failure of payment is not corrected within thirty (30) calendar days after the Transmission Provider notifies the Transmission Customer to cure such failure, a default by the Transmission Customer shall be deemed to exist. Upon the occurrence of a default, the Transmission Provider may initiate a proceeding with the Commission to terminate service but shall not terminate service until the Commission so

approves any such request. In the event of a billing dispute between the Transmission Provider and the Transmission Customer, the Transmission Provider will continue to provide service under the Service Agreement as long as the Transmission Customer (i) continues to make all payments not in dispute, and (ii) pays into an independent escrow account the portion of the invoice in dispute, pending resolution of such dispute. If the Transmission Customer fails to meet these two requirements for continuation of service, then the Transmission Provider may provide notice to the Transmission Customer of its intention to suspend service in sixty (60) days, in accordance with Commission policy.

8 *Accounting for the Transmission Provider's Use of the Tariff*

The Transmission Provider shall record the following amounts, as outlined below.

8.1 Transmission Revenues: Include in a separate operating revenue account or subaccount the revenues it receives from Transmission Service when making Third-Party Sales under Part II of the Tariff.

8.2 Study Costs and Revenues: Include in a separate transmission operating expense account or subaccount, costs properly chargeable to expense that are incurred to perform any System Impact Studies or Facilities Studies which the Transmission Provider conducts to determine if it must construct new transmission facilities or upgrades necessary for its own uses, including making Third-Party Sales under the Tariff; and include in a separate operating revenue account or

subaccount the revenues received for System Impact Studies or Facilities Studies performed when such amounts are separately stated and identified in the Transmission Customer's billing under the Tariff.

9 *Regulatory Filings*

Nothing contained in the Tariff or any Service Agreement shall be construed as affecting in any way the right of the Transmission Provider to unilaterally make application to the Commission for a change in rates, terms and conditions, charges, classification of service, Service Agreement, rule or regulation under Section 205 of the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder.

Nothing contained in the Tariff or any Service Agreement shall be construed as affecting in any way the ability of any Party receiving service under the Tariff to exercise its rights under the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder.

10 *Force Majeure and Indemnification*

10.1 Force Majeure: An event of Force Majeure means any act of God, labor disturbance, act of the public enemy, war, insurrection, riot, fire, storm or flood, explosion, breakage or accident to machinery or equipment, any Curtailment, order, regulation or restriction imposed by governmental military or lawfully established civilian authorities, or any other cause beyond a Party's control. A Force Majeure event does not include an act of negligence or

intentional wrongdoing. Neither the Transmission Provider nor the Transmission Customer will be considered in default as to any obligation under this Tariff if prevented from fulfilling the obligation due to an event of Force Majeure. However, a Party whose performance under this Tariff is hindered by an event of Force Majeure shall make all reasonable efforts to perform its obligations under this Tariff.

10.2 Indemnification: The Transmission Customer shall at all times indemnify, defend, and save the Transmission Provider harmless from, any and all damages, losses, claims, including claims and actions relating to injury to or death of any person or damage to property, demands, suits, recoveries, costs and expenses, court costs, attorney fees, and all other obligations by or to third parties, arising out of or resulting from the Transmission Provider s performance of its obligations under this Tariff on behalf of the Transmission Customer, except in cases of negligence or intentional wrongdoing by the Transmission Provider.

11 *Creditworthiness*

For the purpose of determining the ability of the Transmission Customer to meet its obligations related to service hereunder, the Transmission Provider may require reasonable credit review procedures. This review shall be made in accordance with standard commercial practices. In addition, the Transmission Provider may require the Transmission Customer to provide and maintain in effect during the term of the Service Agreement, an unconditional and irrevocable letter of credit as security to meet its responsibilities and obligations under the Tariff, or an alternative form of security proposed by the Transmission

Customer and acceptable to the Transmission Provider and consistent with commercial practices established by the Uniform Commercial Code that protects the Transmission Provider against the risk of non-payment.

12 *Dispute Resolution Procedures*

12.1 Internal Dispute Resolution Procedures: Any dispute between a **[30,515]** Transmission Customer and the Transmission Provider involving transmission service under the Tariff (excluding applications for rate changes or other changes to the Tariff, or to any Service Agreement entered into under the Tariff, which shall be presented directly to the Commission for resolution) shall be referred to a designated senior representative of the Transmission Provider and a senior representative of the Transmission Customer for resolution on an informal basis as promptly as practicable. In the event the designated representatives are unable to resolve the dispute within thirty (30) days [or such other period as the Parties may agree upon] by mutual agreement, such dispute may be submitted to arbitration and resolved in accordance with the arbitration procedures set forth below.

12.2 External Arbitration Procedures: Any arbitration initiated under the Tariff shall be conducted before a single neutral arbitrator appointed by the Parties. If the Parties fail to agree upon a single arbitrator within ten (10) days of the referral of the dispute to arbitration, each Party shall choose one arbitrator who shall sit on a three-member arbitration panel. The two arbitrators so chosen shall within twenty (20) days select a third arbitrator to chair the arbitration panel. In either case, the arbitrators shall be knowledgeable in electric utility matters, including electric

transmission and bulk power issues, and shall not have any current or past substantial business or financial relationships with any party to the arbitration (except prior arbitration). The arbitrator(s) shall provide each of the Parties an opportunity to be heard and, except as otherwise provided herein, shall generally conduct the arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association and any applicable Commission regulations or Regional Transmission Group rules.

12.3 Arbitration Decisions: Unless otherwise agreed, the arbitrator(s) shall render a decision within ninety (90) days of appointment and shall notify the Parties in writing of such decision and the reasons therefor. The arbitrator(s) shall be authorized only to interpret and apply the provisions of the Tariff and any Service Agreement entered into under the Tariff and shall have no power to modify or change any of the above in any manner. The decision of the arbitrator(s) shall be final and binding upon the Parties, and judgment on the award may be entered in any court having jurisdiction. The decision of the arbitrator(s) may be appealed solely on the grounds that the conduct of the arbitrator(s), or the decision itself, violated the standards set forth in the Federal Arbitration Act and/or the Administrative Dispute Resolution Act. The final decision of the arbitrator must also be filed with the Commission if it affects jurisdictional rates, terms and conditions of service or facilities.

12.4 Costs: Each Party shall be responsible for its own costs incurred during the arbitration process and for the following costs, if applicable:

(A) the cost of the arbitrator chosen by the Party to sit on the three member panel and one half of the cost of the third arbitrator chosen; or

(B) one half the cost of the single arbitrator jointly chosen by the Parties.

12.5 Rights Under The Federal Power Act: Nothing in this section shall restrict the rights of any party to file a Complaint with the Commission under relevant provisions of the Federal Power Act.

II. Point-To-Point Transmission Service

Preamble

The Transmission Provider will provide Firm and Non-Firm Point-To-Point Transmission Service pursuant to the applicable terms and conditions of this Tariff. Point-To-Point Transmission Service is for the receipt of capacity and energy at designated Point(s) of Receipt and the transmission of such capacity and energy to designated Point(s) of Delivery.

13 *Nature of Firm Point-To-Point Transmission Service*

13.1 Term: The minimum term of Firm Point-To-Point Transmission Service shall be one day and the maximum term shall be specified in the Service Agreement.

13.2 Reservation Priority: Long-Term Firm Point-To-Point Transmission Service shall be available on a first-come, **[30,516]** first-served basis *i.e.*, in the chronological

sequence in which each Transmission Customer has reserved service. Reservations for Short-Term Firm Point-To-Point Transmission Service will be conditional based upon the length of the requested transaction. If the Transmission System becomes oversubscribed, requests for longer term service may preempt requests for shorter term service up to the following deadlines: one day before the commencement of daily service, one week before the commencement of weekly service, and one month before the commencement of monthly service. Before the conditional reservation deadline, if available transmission capability is insufficient to satisfy all Applications, an Eligible Customer with a reservation for shorter term service has the right of first refusal to match any longer term reservation before losing its reservation priority. A longer term competing request for Short-Term Firm Point-To-Point Transmission Service will be granted if the Eligible Customer with the right of first refusal does not agree to match the competing request within 24 hours (or earlier if necessary to comply with the scheduling deadlines provided in section 13.8) from being notified by the Transmission Provider of a longer-term competing request for Short-Term Firm Point-To-Point Transmission Service. After the conditional reservation deadline, service will commence pursuant to the terms of Part II of the Tariff. Firm Point-To-Point Transmission Service will always have a reservation priority over Non-Firm Point-To-Point Transmission Service under the Tariff. All Long-Term Firm Point-To-Point Transmission Service will have equal reservation priority with Native Load Customers and Network Customers. Reservation priorities for existing firm service customers are provided in Section 2.2.

13.3 Use of Firm Transmission Service by the Transmission Provider: The Transmission Provider will be subject to the rates, terms and conditions of Part II of the Tariff when making Third-Party Sales under (i) agreements executed on or after [insert date sixty (60) days after publication in Federal Register] or (ii) agreements executed prior to the aforementioned date that the Commission requires to be unbundled, by the date specified by the Commission. The Transmission Provider will maintain separate accounting, pursuant to Section 8, for any use of the Point-To-Point Transmission Service to make Third-Party Sales.

13.4 Service Agreements: The Transmission Provider shall offer a standard form Firm Point-To-Point Transmission Service Agreement (Attachment A) to an Eligible Customer when it submits a Completed Application for Long-Term Firm Point-To-Point Transmission Service. The Transmission Provider shall offer a standard form Firm Point-To-Point Transmission Service Agreement (Attachment A) to an Eligible Customer when it first submits a Completed Application for Short-Term Firm Point-To-Point Transmission Service pursuant to the Tariff. Executed Service Agreements that contain the information required under the Tariff shall be filed (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 40 with the Commission in compliance with applicable Commission regulations.

13.5 Transmission Customer Obligations for Facility Additions or Redispatch Costs: In cases where the Transmission Provider determines that the Transmission System is not capable of providing Firm Point-To-Point Transmission Service without (1) degrading or impairing the

reliability of service to Native Load Customers, Network Customers and other Transmission Customers taking Firm Point-To-Point Transmission Service, or (2) interfering with the Transmission Provider's ability to meet prior firm contractual commitments to others, the Transmission Provider will be obligated to expand or upgrade its Transmission System pursuant to the terms of Section 15.4. The Transmission Customer must agree to compensate the Transmission Provider for any necessary transmission facility additions pursuant to the terms of Section 27. To the extent the Transmission Provider can relieve any system constraint more economically by redispatching the Transmission Provider's resources than through constructing Network Upgrades, it shall do so, provided that the Eligible Customer agrees to compensate the Transmission Provider pursuant to the terms of Section 27. Any redispatch, Network Upgrade **[30,517]** or Direct Assignment Facilities costs (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 41 to be charged to the Transmission Customer on an incremental basis under the Tariff will be specified in the Service Agreement prior to initiating service.

13.6 Curtailment of Firm Transmission Service: In the event that a Curtailment on the Transmission Provider's Transmission System, or a portion thereof, is required to maintain reliable operation of such system, Curtailments will be made on a non-discriminatory basis to the transaction(s) that effectively relieve the constraint. If multiple transactions require Curtailment, to the extent practicable and consistent with Good Utility Practice, the Transmission Provider will curtail service to Network Customers and Transmission Customers taking Firm Point-To-Point Transmission Service on a basis comparable to the curtailment of service to the

Transmission Provider's Native Load Customers. All Curtailments will be made on a non-discriminatory basis, however, Non-Firm Point-To-Point Transmission Service shall be subordinate to Firm Transmission Service. When the Transmission Provider determines that an electrical emergency exists on its Transmission System and implements emergency procedures to Curtail Firm Transmission Service, the Transmission Customer shall make the required reductions upon request of the Transmission Provider. However, the Transmission Provider reserves the right to Curtail, in whole or in part, any Firm Transmission Service provided under the Tariff when, in the Transmission Provider's sole discretion, an emergency or other unforeseen condition impairs or degrades the reliability of its Transmission System. The Transmission Provider will notify all affected Transmission Customers in a timely manner of any scheduled Curtailments.

13.7 Classification of Firm Transmission Service:

(a) The Transmission Customer taking Firm Point-To- Point Transmission Service may (1) change its Receipt and Delivery Points to obtain service on a non-firm basis consistent with the terms of Section 22.1 or (2) request a modification of the Points of Receipt or Delivery on a firm basis pursuant to the terms of Section 22.2.

(b) The Transmission Customer may purchase transmission service to make sales of capacity and energy from multiple generating units that are on the Transmission Provider's Transmission System. For such a purchase of transmission service, the resources will be designated as multiple Points of Receipt, unless the multiple generating

units are at the same generating plant in which case the units would be treated as a single Point of Receipt.

(c) The Transmission Provider shall provide firm deliveries of capacity and energy from the Point(s) of Receipt to the Point(s) of Delivery. Each Point of Receipt at which firm transmission capacity is reserved by the Transmission Customer shall be set forth in the Firm Point-To-Point Service Agreement for Long-Term Firm Transmission Service along with a corresponding capacity reservation associated with each Point of Receipt. Points of Receipt and corresponding capacity reservations shall be as mutually agreed upon by the Parties for Short-Term Firm Transmission. Each Point of Delivery at which firm transmission capacity is reserved by the Transmission Customer shall be set forth in the Firm Point-To-Point Service Agreement for Long-Term Firm Transmission Service along with a corresponding capacity reservation associated with each Point of Delivery. Points of Delivery and corresponding capacity reservations shall be as mutually agreed upon by the Parties for Short-Term Firm Transmission. The greater of either (1) the sum of the capacity reservations at the Point(s) of Receipt, or (2) the sum of the capacity reservations at the Point(s) of Delivery shall be the Transmission Customer's Reserved Capacity. The Transmission Customer will be billed for its Reserved Capacity under the terms of Schedule 7. The Transmission Customer may not exceed its firm capacity reserved at each Point of Receipt and each Point of Delivery except as otherwise specified in Section 22. The Transmission Provider shall specify the rate treatment and all related terms and conditions applicable in the event that a Transmission Customer (including Third-Party Sales by the Transmission

Provider) **[30,518]** exceeds its firm reserved capacity at any Point of Receipt or Point of Delivery.

13.8 Scheduling of Firm Point-To-Point Transmission Service: Schedules for the Transmission Customer's Firm Point-To-Point Transmission Service must be submitted to the Transmission Provider no later than 10:00 a.m. [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] of the day prior to commencement of such service. Schedules submitted after 10:00 a.m. will be accommodated, if practicable. Hour-to-hour schedules of any capacity and energy that is to be delivered must be stated in increments of 1,000 kW per hour [or a reasonable increment that is generally accepted in the region and is consistently adhered to by the Transmission Provider]. Transmission Customers within the Transmission Provider's service area with multiple requests for Transmission Service at a Point of Receipt, each of which is under 1,000 kW per hour, may consolidate their service requests at a common point of receipt into units of 1,000 kW per hour for scheduling and billing purposes. Scheduling changes will be permitted up to twenty (20) minutes [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] before the start of the next clock hour provided that the Delivering Party and Receiving Party also agree to the schedule modification. The Transmission Provider will furnish to the Delivering Party's system operator, hour-to-hour schedules equal to those furnished by the Receiving Party (unless reduced for losses) and shall deliver the capacity and energy provided by such schedules. Should the Transmission Customer, Delivering Party or Receiving Party revise or terminate any schedule, such party shall immediately

notify the Transmission Provider, and the Transmission Provider shall have the right to adjust accordingly the schedule for capacity and energy to be received and to be delivered.

14 *Nature of Non-Firm Point-To-Point Transmission Service*

14.1 Term: Non-Firm Point-To-Point Transmission Service will be available for periods ranging from one (1) hour to one (1) month. However, a Purchaser of Non-Firm Point-To-Point Transmission Service will be entitled to reserve a sequential term of service (such as a sequential monthly term without having to wait for the initial term to expire before requesting another monthly term) so that the total time period for which the reservation applies is greater than one month, subject to the requirements of Section 18.3.

14.2 Reservation Priority: Non-Firm Point-To-Point Transmission Service shall be available from transmission capability in excess of that needed for reliable service to Native Load Customers, Network Customers and other Transmission Customers taking Long- Term and Short-Term Firm Point-To-Point Transmission Service. A higher priority will be assigned to reservations with a longer duration of service. In the event the Transmission System is constrained, competing requests of equal duration will be prioritized based on the highest price offered by the Eligible Customer for the Transmission Service. Eligible Customers that have already reserved shorter term service have the right of first refusal to match any longer term reservation before being preempted. A longer term competing request for Non-Firm Point-To-Point Transmission Service will be granted if the Eligible Customer with the right of first refusal does not agree to match the

competing request: (a) immediately for hourly Non-Firm Point-To-Point Transmission Service after notification by the Transmission Provider; and, (b) within 24 hours (or earlier if necessary to comply with the scheduling deadlines provided in section 14.6) for Non-Firm Point-To-Point Transmission Service other than hourly transactions after notification by the Transmission Provider. Transmission service for Network Customers from resources other than designated Network Resources will have a higher priority than any Non-Firm Point-To-Point Transmission Service. Non-Firm Point-To-Point Transmission Service over secondary Point(s) of Receipt and Point(s) of Delivery will have the lowest reservation priority under the Tariff.

14.3 Use of Non-Firm Point-To-Point Transmission Service by the [30,519] Transmission Provider: The Transmission Provider will be subject to the rates, terms and conditions of Part II of the Tariff when making Third-Party Sales under (i) agreements executed on or after [insert date (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 48 sixty (60) days after publication in Federal Register] or (ii) agreements executed prior to the aforementioned date that the Commission requires to be unbundled, by the date specified by the Commission. The Transmission Provider will maintain separate accounting, pursuant to Section 8, for any use of Non-Firm Point-To-Point Transmission Service to make Third-Party Sales.

14.4 Service Agreements: The Transmission Provider shall offer a standard form Non-Firm Point-To-Point Transmission Service Agreement (Attachment B) to an Eligible Customer when it first submits a Completed Application for Non-Firm Point-To-Point Transmission

Service pursuant to the Tariff. Executed Service Agreements that contain the information required under the Tariff shall be filed with the Commission in compliance with applicable Commission regulations.

14.5 Classification of Non-Firm Point-To-Point Transmission Service: Non-Firm Point-To-Point Transmission Service shall be offered under terms and conditions contained in Part II of the Tariff. The Transmission Provider undertakes no obligation under the Tariff to plan its Transmission System in order to have sufficient capacity for Non-Firm Point-To-Point Transmission Service. Parties requesting Non-Firm Point-To-Point Transmission Service for the transmission of firm power do so with the full realization that such service is subject to availability and to Curtailment or Interruption under the terms of the Tariff. The Transmission Provider shall specify the rate treatment and all related terms and conditions applicable in the event that a Transmission Customer (including Third- Party Sales by the Transmission Provider) exceeds its non-firm capacity reservation. Non-Firm Point-To-Point Transmission Service shall include transmission of energy on an hourly basis and transmission of scheduled short-term capacity and energy on a daily, weekly or monthly basis, but not to exceed one month's reservation for any one Application, under Schedule 8.

14.6 Scheduling of Non-Firm Point-To-Point Transmission Service: Schedules for Non-Firm Point-To-Point Transmission Service must be submitted to the Transmission Provider no later than *2:00 p.m.* [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] of the

day prior to commencement of such service. Schedules submitted after 2:00 p.m. will be accommodated, if practicable. Hour-to-hour schedules of energy that is to be delivered must be stated in increments of 1,000 kW per hour [or a reasonable increment that is generally accepted in the region and is consistently adhered to by the Transmission Provider]. Transmission Customers within the Transmission Provider's service area with multiple requests for Transmission Service at a Point of Receipt, each of which is under 1,000 kW per hour, may consolidate their schedules at a common Point of Receipt into units of 1,000 kW per hour. Scheduling changes will be permitted up to *twenty (20) minutes* [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] before the start of the next clock hour provided that the Delivering Party and Receiving Party also agree to the schedule modification. The Transmission Provider will furnish to the Delivering Party's system operator, hour-to-hour schedules equal to those furnished by the Receiving Party (unless reduced for losses) and shall deliver the capacity and energy provided by such schedules. Should the Transmission Customer, Delivering Party or Receiving Party revise or terminate any schedule, such party shall immediately notify the Transmission Provider, and the Transmission Provider shall have the right to adjust accordingly the schedule for capacity and energy to be received and to be delivered.

14.7 Curtailment or Interruption of Service: The Transmission Provider reserves the right to Curtail, in whole or in part, Non-Firm Point-To-Point Transmission Service provided under the Tariff for reliability reasons when, an emergency or other unforeseen condition threatens to impair

or degrade **[30,520]** the reliability of its Transmission System. The Transmission Provider reserves the right to Interrupt, in whole or in part, Non-Firm Point-To-Point Transmission Service provided under the Tariff for economic reasons in order to accommodate (1) a request for Firm Transmission Service, (2) a request for Non- Firm Point-To-Point Transmission Service of greater duration, (3) a request for Non-Firm Point-To-Point Transmission Service of equal duration with a higher price, or (4) transmission service for Network Customers from non-designated resources. The Transmission Provider also will discontinue or reduce service to the Transmission Customer to the extent that deliveries for transmission are discontinued or reduced at the Point(s) of Receipt. Where required, Curtailments or Interruptions will be made on a non- discriminatory basis to the transaction(s) that effectively relieve the constraint, however, Non-Firm Point-To-Point Transmission Service shall be subordinate to Firm Transmission Service. If multiple transactions require Curtailment or Interruption, to the extent practicable and consistent with Good Utility Practice, Curtailments or Interruptions will be made to transactions of the shortest term (*e.g.*, hourly non- firm transactions will be Curtailed or Interrupted before daily non-firm transactions and daily non-firm transactions will be Curtailed or Interrupted before weekly non-firm transactions). Transmission service for Network Customers from resources other than designated Network Resources will have a higher priority than any Non-Firm Point-To-Point Transmission Service under the Tariff. Non-Firm Point-To-Point Transmission Service over secondary Point(s) of Receipt and Point(s) of Delivery will have a lower priority than any Non-Firm Point-To-Point Transmission Service under the Tariff. The Transmission Provider will provide advance notice of Curtailment or

Interruption where such notice can be provided consistent with Good Utility Practice.

15 *Service Availability*

15.1 General Conditions: The Transmission Provider will provide Firm and Non-Firm Point-To-Point Transmission Service over, on or across its Transmission System to any Transmission Customer that has met the requirements of Section 16.

15.2 Determination of Available Transmission Capability: A description of the Transmission Provider's specific methodology for assessing available transmission capability posted on the Transmission Provider's OASIS (Section 4) is contained in Attachment C of the Tariff. In the event sufficient transmission capability may not exist to accommodate a service request, the Transmission Provider will respond by performing a System Impact Study.

15.3 Initiating Service in the Absence of an Executed Service Agreement: If the Transmission Provider and the Transmission Customer requesting Firm or Non-Firm Point-To-Point Transmission Service cannot agree on all the terms and conditions of the Point-To-Point Service Agreement, the Transmission Provider shall file with the Commission, within thirty (30) days after the date the Transmission Customer provides written notification directing the Transmission Provider to file, an unexecuted Point-To-Point Service Agreement containing terms and conditions deemed appropriate by the Transmission Provider for such requested Transmission Service. The Transmission Provider shall commence providing Transmission Service subject to the

Transmission Customer agreeing to (i) compensate the Transmission Provider at whatever rate the Commission ultimately determines to be just and reasonable, and (ii) comply with the terms and conditions of the Tariff including posting appropriate security deposits in accordance with the terms of Section 17.3.

15.4 Obligation to Provide Transmission Service that Requires Expansion or Modification of the Transmission System: If the Transmission Provider determines that it cannot accommodate a Completed Application for Firm Point-To-Point Transmission Service because of insufficient capability on its Transmission System, the Transmission Provider will use due diligence to expand or modify its Transmission System to provide the requested Firm Transmission Service, provided the Transmission Customer agrees to compensate the Transmission **[30,521]** Provider for such costs pursuant to the terms of Section 27. The Transmission Provider will conform to Good Utility Practice in determining the need for new facilities and in the design and construction of such facilities. The obligation applies only to those facilities that the Transmission Provider has the right to expand or modify.

15.5 Deferral of Service: The Transmission Provider may defer providing service until it completes construction of new transmission facilities or upgrades needed to provide Firm Point-To-Point Transmission Service whenever the Transmission Provider determines that providing the requested service would, without such new facilities or upgrades, impair or degrade reliability to any existing firm services.

15.6 Other Transmission Service Schedules: Eligible Customers receiving transmission service under other agreements on file with the Commission may continue to receive transmission service under those agreements until such time as those agreements may be modified by the Commission.

15.7 Real Power Losses: Real Power Losses are associated with all transmission service. The Transmission Provider is not obligated to provide Real Power Losses. The Transmission Customer is responsible for replacing losses associated with all transmission service as calculated by the Transmission Provider. The applicable Real Power Loss factors are as follows: [To be completed by the Transmission Provider].

16 *Transmission Customer Responsibilities*

16.1 Conditions Required of Transmission Customers: Point-To-Point Transmission Service shall be provided by the Transmission Provider only if the following conditions are satisfied by the Transmission Customer:

a. The Transmission Customer has pending a Completed Application for service;

b. The Transmission Customer meets the creditworthiness criteria set forth in Section 11;

c. The Transmission Customer will have arrangements in place for any other transmission service necessary to effect the delivery from the generating source to

the Transmission Provider prior to the time service under Part II of the Tariff commences;

d. The Transmission Customer agrees to pay for any facilities constructed and chargeable to such Transmission Customer under Part II of the Tariff, whether or not the Transmission Customer takes service for the full term of its reservation; and

e. The Transmission Customer has executed a Point-To- Point Service Agreement or has agreed to receive service pursuant to Section 15.3.

16.2 Transmission Customer Responsibility for Third-Party Arrangements: Any scheduling arrangements that may be required by other electric systems shall be the responsibility of the Transmission Customer requesting service. The Transmission Customer shall provide, unless waived by the Transmission Provider, notification to the Transmission Provider identifying such systems and authorizing them to schedule the capacity and energy to be transmitted by the Transmission Provider pursuant to Part II of the Tariff on behalf of the Receiving Party at the Point of Delivery or the Delivering Party at the Point of Receipt. However, the Transmission Provider will undertake reasonable efforts to assist the Transmission Customer in making such arrangements, including without limitation, providing any information or data required by such other electric system pursuant to Good Utility Practice.

17 *Procedures for Arranging Firm Point-To-Point Transmission Service*

17.1 Application: A request for Firm Point-To-Point Transmission Service for periods of one year or longer must contain a written Application to: [Transmission Provider Name and Address], at least sixty (60) days in advance of the calendar month in which service is to commence. The Transmission Provider will consider requests for such firm service on shorter notice when feasible. Requests for firm service for periods of less than one year shall be subject to expedited procedures that shall be negotiated between the Parties within the time constraints provided in Section 17.5. All Firm Point-To-Point Transmission Service requests should **[30,522]** be submitted by entering the information listed below on the Transmission Provider's OASIS. Prior to implementation of the Transmission Provider's OASIS, a Completed Application may be submitted by (i) transmitting the required information to the Transmission Provider by telefax, or (ii) providing the information by telephone over the Transmission Provider's time recorded telephone line. Each of these methods will provide a time-stamped record for establishing the priority of the Application.

17.2 Completed Application: A Completed Application shall provide all of the information included in 18 CFR 2.20 including but not limited to the following:

(i) The identity, address, telephone number and facsimile number of the entity requesting service;

(ii) A statement that the entity requesting service is, or will be upon commencement of service, an Eligible Customer under the Tariff;

(iii) The location of the Point(s) of Receipt and Point(s) of Delivery and the identities of the Delivering Parties and the Receiving Parties;

(iv) The location of the generating facility(ies) supplying the capacity and energy and the location of the load ultimately served by the capacity and energy transmitted. The Transmission Provider will treat this information as confidential except to the extent that disclosure of this information is required by this Tariff, by regulatory or judicial order, for reliability purposes pursuant to Good Utility Practice or pursuant to RTG transmission information sharing agreements. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations;

(v) A description of the supply characteristics of the capacity and energy to be delivered;

(vi) An estimate of the capacity and energy expected to be delivered to the Receiving Party;

(vii) The Service Commencement Date and the term of the requested Transmission Service; and

(viii) The transmission capacity requested for each Point of Receipt and each Point of Delivery on the Transmission Provider's Transmission System; customers may combine their requests for service in order to satisfy the

minimum transmission capacity requirement. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations.

17.3 Deposit: A Completed Application for Firm Point-To-Point Transmission Service also shall include a deposit of either one month's charge for Reserved Capacity or the full charge for Reserved Capacity for service requests of less than one month. If the Application is rejected by the Transmission Provider because it does not meet the conditions for service as set forth herein, or in the case of requests for service arising in connection with losing bidders in a Request For Proposals (RFP), said deposit shall be returned with interest less any reasonable costs incurred by the Transmission Provider in connection with the review of the losing bidder's Application. The deposit also will be returned with interest less any reasonable costs incurred by the Transmission Provider if the Transmission Provider is unable to complete new facilities needed to provide the service. If an Application is withdrawn or the Eligible Customer decides not to enter into a Service Agreement for Firm Point-To-Point Transmission Service, the deposit shall be refunded in full, with interest, less reasonable costs incurred by the Transmission Provider to the extent such costs have not already been recovered by the Transmission Provider from the Eligible Customer. The Transmission Provider will provide to the Eligible Customer a complete accounting of all costs deducted from the refunded deposit, which the Eligible Customer may contest if there is a dispute concerning the deducted costs. Deposits associated with construction of new facilities are subject to the provisions of Section 19. If a Service Agreement for Firm Point-To-Point Transmission

Service is executed, the deposit, with interest, will be returned to the Transmission Customer upon expiration **[30,523]** or termination of the Service Agreement for Firm Point-To-Point Transmission Service. Applicable interest shall be computed in accordance with the Commission's regulations at 18 CFR §35.19a(a)(2)(iii), and shall be calculated from the day the deposit check is credited to the Transmission Provider's account.

17.4 Notice of Deficient Application: If an Application fails to meet the requirements of the Tariff, the Transmission Provider shall notify the entity requesting service within fifteen (15) days of receipt of the reasons for such failure. The Transmission Provider will attempt to remedy minor deficiencies in the Application through informal communications with the Eligible Customer. If such efforts are unsuccessful, the Transmission Provider shall return the Application, along with any deposit, with interest. Upon receipt of a new or revised Application that fully complies with the requirements of Part II of the Tariff, the Eligible Customer shall be assigned a new priority consistent with the date of the new or revised Application.

17.5 Response to a Completed Application: Following receipt of a Completed Application for Firm Point-To-Point Transmission Service, the Transmission Provider shall make a determination of available transmission capability as required in Section 15.2. The Transmission Provider shall notify the Eligible Customer as soon as practicable, but not later than thirty (30) days after the date of receipt of a Completed Application either (i) if it will be able to provide service without performing a System Impact Study or (ii) if such a study is needed to evaluate the impact of the

Application pursuant to Section 19.1. Responses by the Transmission Provider must be made as soon as practicable to all completed applications (including applications by its own merchant function) and the timing of such responses must be made on a non-discriminatory basis.

17.6 Execution of Service Agreement: Whenever the Transmission Provider determines that a System Impact Study is not required and that the service can be provided, it shall notify the Eligible Customer as soon as practicable but no later than thirty (30) days after receipt of the Completed Application. Where a System Impact Study is required, the provisions of Section 19 will govern the execution of a Service Agreement. Failure of an Eligible Customer to execute and return the Service Agreement or request the filing of an unexecuted service agreement pursuant to Section 15.3, within fifteen (15) days after it is tendered by the Transmission Provider will be deemed a withdrawal and termination of the Application and any deposit submitted shall be refunded with interest. Nothing herein limits the right of an Eligible Customer to file another Application after such withdrawal and termination.

17.7 Extensions for Commencement of Service: The Transmission Customer can obtain up to *five (5) one-year extensions* for the commencement of service. The Transmission Customer may postpone service by paying a non-refundable annual reservation fee equal to one- month's charge for Firm Transmission Service for each year or fraction thereof. If during any extension for the commencement of service an Eligible Customer submits a Completed Application for Firm Transmission Service, and such request can be satisfied only by releasing all or part of

the Transmission Customer's Reserved Capacity, the original Reserved Capacity will be released unless the following condition is satisfied. Within thirty (30) days, the original Transmission Customer agrees to pay the Firm Point-To-Point transmission rate for its Reserved Capacity concurrent with the new Service Commencement Date. In the event the Transmission Customer elects to release the Reserved Capacity, the reservation fees or portions thereof previously paid will be forfeited.

18 *Procedures for Arranging Non-Firm Point-To-Point Transmission Service*

18.1 Application: Eligible Customers seeking Non-Firm Point-To-Point Transmission Service must submit a Completed Application to the Transmission Provider. Applications should be submitted by entering the information listed below on the Transmission Provider's OASIS. Prior to implementation of the Transmission Provider's OASIS, a Completed Application may be submitted by (i) transmitting the required **[30,524]** information to the Transmission Provider by telefax, or (ii) providing the information by telephone over the Transmission Provider's time recorded telephone line. Each of these methods will provide a time-stamped record for establishing the service priority of the Application.

18.2 Completed Application: A Completed Application shall provide all of the information included in 18 CFR §2.20 including but not limited to the following:

(i) The identity, address, telephone number and facsimile number of the entity requesting service;

(ii) A statement that the entity requesting service is, or will be upon commencement of service, an Eligible Customer under the Tariff;

(iii) The Point(s) of Receipt and the Point(s) of Delivery;

(iv) The maximum amount of capacity requested at each Point of Receipt and Point of Delivery; and

(v) The proposed dates and hours for initiating and terminating transmission service hereunder.

In addition to the information specified above, when required to properly evaluate system conditions, the Transmission Provider also may ask the Transmission Customer to provide the following:

(vi) The electrical location of the initial source of the power to be transmitted pursuant to the Transmission Customer's request for service; and

(vii) The electrical location of the ultimate load.

The Transmission Provider will treat this information in (vi) and (vii) as confidential at the request of the Transmission Customer except to the extent that disclosure of this information is required by this Tariff, by regulatory or judicial order, for reliability purposes pursuant to Good Utility Practice, or pursuant to RTG transmission information sharing agreements. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations.

18.3 Reservation of Non-Firm Point-To-Point Transmission Service: Requests for monthly service shall be submitted *no earlier than sixty (60) days* before service is to commence; requests for weekly service shall be submitted *no earlier than fourteen (14) days* before service is to commence, requests for daily service shall be submitted *no earlier than two (2) days* before service is to commence, and requests for hourly service shall be submitted *no earlier than noon the day* before service is to commence. Requests for service received later than *2:00 p.m.* prior to the day service is scheduled to commence will be accommodated if practicable [or such reasonable times that are generally accepted in the region and are consistently adhered to by the Transmission Provider].

18.4 Determination of Available Transmission Capability: Following receipt of a tendered schedule the Transmission Provider will make a determination on a non-discriminatory basis of available transmission capability pursuant to Section 15.2. Such determination shall be made as soon as reasonably practicable after receipt, but not later than the following time periods for the following terms of service *(i) thirty (30) minutes for hourly service, (ii) thirty (30) minutes for daily service, (iii) four (4) hours for weekly service, and (iv) two (2) days for monthly service.* [Or such reasonable times that are generally accepted in the region and are consistently adhered to by the Transmission Provider].

19 *Additional Study Procedures For Firm Point-To-Point Transmission Service Requests*

19.1 Notice of Need for System Impact Study: After receiving a request for service, the Transmission Provider shall determine on a non-discriminatory basis whether a

System Impact Study is needed. A description of the Transmission Provider's methodology for completing a System Impact Study is provided in Attachment D. If the Transmission Provider determines that a System Impact Study is necessary to accommodate the requested service, it shall so inform the Eligible Customer, as soon as practicable. In such cases, the Transmission Provider shall within thirty (30) days of receipt of a Completed Application, tender a System Impact Study Agreement pursuant to which the Eligible Customer shall agree **[30,525]** to reimburse the Transmission Provider for performing the required System Impact Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the System Impact Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the System Impact Study Agreement, its application shall be deemed withdrawn and its deposit, pursuant to Section 17.3, shall be returned with interest.

19.2 System Impact Study Agreement and Cost Reimbursement:

(i) The System Impact Study Agreement will clearly specify the Transmission Provider's estimate of the actual cost, and time for completion of the System Impact Study. The charge shall not exceed the actual cost of the study. In performing the System Impact Study, the Transmission Provider shall rely, to the extent reasonably practicable, on existing transmission planning studies. The Eligible Customer will not be assessed a charge for such existing studies; however, the Eligible Customer will be responsible for charges associated with any modifications to existing planning studies that are reasonably necessary to

evaluate the impact of the Eligible Customer's request for service on the Transmission System.

(ii) If in response to multiple Eligible Customers requesting service in relation to the same competitive solicitation, a single System Impact Study is sufficient for the Transmission Provider to accommodate the requests for service, the costs of that study shall be pro-rated among the Eligible Customers.

(iii) For System Impact Studies that the Transmission Provider conducts on its own behalf, the Transmission Provider shall record the cost of the System Impact Studies pursuant to Section 20.

19.3 System Impact Study Procedures: Upon receipt of an executed System Impact Study Agreement, the Transmission Provider will use due diligence to complete the required System Impact Study within a sixty (60) day period. The System Impact Study shall identify any system constraints and redispatch options, additional Direct Assignment Facilities or Network Upgrades required to provide the requested service. In the event that the Transmission Provider is unable to complete the required System Impact Study within such time period, it shall so notify the Eligible Customer and provide an estimated completion date along with an explanation of the reasons why additional time is required to complete the required studies. A copy of the completed System Impact Study and related work papers shall be made available to the Eligible Customer. The Transmission Provider will use the same due diligence in completing the System Impact Study for an Eligible Customer as it uses when completing studies for itself. The Transmission Provider shall

notify the Eligible Customer immediately upon completion of the System Impact Study if the Transmission System will be adequate to accommodate all or part of a request for service or that no costs are likely to be incurred for new transmission facilities or upgrades. In order for a request to remain a Completed Application, within fifteen (15) days of completion of the System Impact Study the Eligible Customer must execute a Service Agreement or request the filing of an unexecuted Service Agreement pursuant to Section 15.3, or the Application shall be deemed terminated and withdrawn.

19.4 Facilities Study Procedures: If a System Impact Study indicates that additions or upgrades to the Transmission System are needed to supply the Eligible Customer's service request, the Transmission Provider, within thirty (30) days of the completion of the System Impact Study, shall tender to the Eligible Customer a Facilities Study Agreement pursuant to which the Eligible Customer shall agree to reimburse the Transmission Provider for performing the required Facilities Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the Facilities Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the Facilities Study Agreement, its application shall be deemed withdrawn and its deposit, pursuant to Section 17.3, shall be returned **[30,526]** with interest. Upon receipt of an executed Facilities Study Agreement, the Transmission Provider will use due diligence to complete the required Facilities Study within a sixty (60) day period. If the Transmission Provider is unable to complete the Facilities Study in the allotted time period, the Transmission Provider shall notify the Transmission Customer and provide an estimate of the time needed to reach a final determination

along with an explanation of the reasons that additional time is required to complete the study. When completed, the Facilities Study will include a good faith estimate of (i) the cost of Direct Assignment Facilities to be charged to the Transmission Customer, (ii) the Transmission Customer's appropriate share of the cost of any required Network Upgrades as determined pursuant to the provisions of Part II of the Tariff, and (iii) the time required to complete such construction and initiate the requested service. The Transmission Customer shall provide the Transmission Provider with a letter of credit or other reasonable form of security acceptable to the Transmission Provider equivalent to the costs of new facilities or upgrades consistent with commercial practices as established by the Uniform Commercial Code. The Transmission Customer shall have thirty (30) days to execute a Service Agreement or request the filing of an unexecuted Service Agreement and provide the required letter of credit or other form of security or the request will no longer be a Completed Application and shall be deemed terminated and withdrawn.

19.5 Facilities Study Modifications: Any change in design arising from inability to site or construct facilities as proposed will require development of a revised good faith estimate. New good faith estimates also will be required in the event of new statutory or regulatory requirements that are effective before the completion of construction or other circumstances beyond the control of the Transmission Provider that significantly affect the final cost of new facilities or upgrades to be charged to the Transmission Customer pursuant to the provisions of Part II of the Tariff.

19.6 Due Diligence in Completing New Facilities: The Transmission Provider shall use due diligence to add necessary facilities or upgrade its Transmission System within a reasonable time. The Transmission Provider will not upgrade its existing or planned Transmission System in order to provide the requested Firm Point-To-Point Transmission Service if doing so would impair system reliability or otherwise impair or degrade existing firm service.

19.7 Partial Interim Service: If the Transmission Provider determines that it will not have adequate transmission capability to satisfy the full amount of a Completed Application for Firm Point-To-Point Transmission Service, the Transmission Provider nonetheless shall be obligated to offer and provide the portion of the requested Firm Point-To-Point Transmission Service that can be accommodated without addition of any facilities and through redispatch. However, the Transmission Provider shall not be obligated to provide the incremental amount of requested Firm Point-To-Point Transmission Service that requires the addition of facilities or upgrades to the Transmission System until such facilities or upgrades have been placed in service.

19.8 Expedited Procedures for New Facilities: In lieu of the procedures set forth above, the Eligible Customer shall have the option to expedite the process by requesting the Transmission Provider to tender at one time, together with the results of required studies, an "Expedited Service Agreement" pursuant to which the Eligible Customer would agree to compensate the Transmission Provider for all costs incurred pursuant to the terms of the Tariff. In order to exercise this option, the Eligible Customer shall request in writing an expedited Service Agreement covering all of the above-

specified items within thirty (30) days of receiving the results of the System Impact Study identifying needed facility additions or upgrades or costs incurred in providing the requested service. While the Transmission Provider agrees to provide the Eligible Customer with its best estimate of the new facility costs and other charges that may be incurred, such estimate shall not be binding and the Eligible Customer must agree in writing to compensate the Transmission Provider **[30,527]** for all costs incurred pursuant to the provisions of the Tariff. The Eligible Customer shall execute and return such an Expedited Service Agreement within fifteen (15) days of its receipt or the Eligible Customer's request for service will cease to be a Completed Application and will be deemed terminated and withdrawn.

20 Procedures if The Transmission Provider is Unable to Complete New Transmission Facilities for Firm Point-To-Point Transmission Service

20.1 Delays in Construction of New Facilities: If any event occurs that will materially affect the time for completion of new facilities, or the ability to complete them, the Transmission Provider shall promptly notify the Transmission Customer. In such circumstances, the Transmission Provider shall within thirty (30) days of notifying the Transmission Customer of such delays, convene a technical meeting with the Transmission Customer to evaluate the alternatives available to the Transmission Customer. The Transmission Provider also shall make available to the Transmission Customer studies and work papers related to the delay, including all information that is in the possession of the Transmission Provider that is reasonably needed by the Transmission Customer to evaluate any alternatives.

20.2 Alternatives to the Original Facility Additions: When the review process of Section 20.1 determines that one or more alternatives exist to the originally planned construction project, the Transmission Provider shall present such alternatives for consideration by the Transmission Customer. If, upon review of any alternatives, the Transmission Customer desires to maintain its Completed Application subject to construction of the alternative facilities, it may request the Transmission Provider to submit a revised Service Agreement for Firm Point-To-Point Transmission Service. If the alternative approach solely involves Non-Firm Point-To-Point Transmission Service, the Transmission Provider shall promptly tender a Service Agreement for Non-Firm Point-To-Point Transmission Service providing for the service. In the event the Transmission Provider concludes that no reasonable alternative exists and the Transmission Customer disagrees, the Transmission Customer may seek relief under the dispute resolution procedures pursuant to Section 12 or it may refer the dispute to the Commission for resolution.

20.3 Refund Obligation for Unfinished Facility Additions: If the Transmission Provider and the Transmission Customer mutually agree that no other reasonable alternatives exist and the requested service cannot be provided out of existing capability under the conditions of Part II of the Tariff, the obligation to provide the requested Firm Point-To-Point Transmission Service shall terminate and any deposit made by the Transmission Customer shall be returned with interest pursuant to Commission regulations 35.19a(a)(2)(iii). However, the Transmission Customer shall be responsible for all prudently incurred costs by the Transmission Provider through the time construction was suspended.

21 *Provisions Relating to Transmission Construction and Services on the Systems of Other Utilities*

21.1 Responsibility for Third-Party System Additions: The Transmission Provider shall not be responsible for making arrangements for any necessary engineering, permitting, and construction of transmission or distribution facilities on the system(s) of any other entity or for obtaining any regulatory approval for such facilities. The Transmission Provider will undertake reasonable efforts to assist the Transmission Customer in obtaining such arrangements, including without limitation, providing any information or data required by such other electric system pursuant to Good Utility Practice.

21.2 Coordination of Third-Party System Additions: In circumstances where the need for transmission facilities or upgrades is identified pursuant to the provisions of Part II of the Tariff, and if such upgrades further require the addition of transmission facilities on other systems, the Transmission Provider shall have the right to coordinate construction on its own system with the construction required by others. The Transmission Provider, after consultation with the Transmission Customer and representatives of such **[50,528]** other systems, may defer construction of its new transmission facilities, if the new transmission facilities on another system cannot be completed in a timely manner. The Transmission Provider shall notify the Transmission Customer in writing of the basis for any decision to defer construction and the specific problems which must be resolved before it will initiate or resume construction of new facilities. Within sixty (60) days of receiving written notification by the Transmission Provider of its intent to defer construction pursuant to this

section, the Transmission Customer may challenge the decision in accordance with the dispute resolution procedures pursuant to Section 12 or it may refer the dispute to the Commission for resolution.

22 *Changes in Service Specifications*

22.1 Modifications On a Non-Firm Basis: The Transmission Customer taking Firm Point-To-Point Transmission Service may request the Transmission Provider to provide transmission service on a non-firm basis over Receipt and Delivery Points other than those specified in the Service Agreement ("Secondary Receipt and Delivery Points"), in amounts not to exceed its firm capacity reservation, without incurring an additional Non-Firm Point-To-Point Transmission Service charge or executing a new Service Agreement, subject to the following conditions.

(a) Service provided over Secondary Receipt and Delivery Points will be non-firm only, on an as- available basis and will not displace any firm or non-firm service reserved or scheduled by third-parties under the Tariff or by the Transmission Provider on behalf of its Native Load Customers.

(b) The sum of all Firm and non-firm Point-To-Point Transmission Service provided to the Transmission Customer at any time pursuant to this section shall not exceed the Reserved Capacity in the relevant Service Agreement under which such services are provided.

(c) The Transmission Customer shall retain its right to schedule Firm Point-To-Point Transmission Service

at the Receipt and Delivery Points specified in the relevant Service Agreement in the amount of its original capacity reservation.

(d) Service over Secondary Receipt and Delivery Points on a non-firm basis shall not require the filing of an Application for Non-Firm Point-To-Point Transmission Service under the Tariff. However, all other requirements of Part II of the Tariff (except as to transmission rates) shall apply to transmission service on a non-firm basis over Secondary Receipt and Delivery Points.

22.2 Modification On a Firm Basis: Any request by a Transmission Customer to modify Receipt and Delivery Points on a firm basis shall be treated as a new request for service in accordance with Section 17 hereof, except that such Transmission Customer shall not be obligated to pay any additional deposit if the capacity reservation does not exceed the amount reserved in the existing Service Agreement. While such new request is pending, the Transmission Customer shall retain its priority for service at the existing firm Receipt and Delivery Points specified in its Service Agreement.

23 *Sale or Assignment of Transmission Service*

23.1 Procedures for Assignment or Transfer of Service: Subject to Commission approval of any necessary filings, a Transmission Customer may sell, assign, or transfer all or a portion of its rights under its Service Agreement, but only to another Eligible Customer (the Assignee). The Transmission Customer that sells, assigns or transfers its rights under its Service Agreement is hereafter referred to as the Reseller. Compensation to the Reseller shall not exceed

the higher of (i) the original rate paid by the Reseller, (ii) the Transmission Provider's maximum rate on file at the time of the assignment, or (iii) the Reseller's opportunity cost capped at the Transmission Provider's cost of expansion. If the Assignee does not request any change in the Point(s) of Receipt or the Point(s) of Delivery, or a change in any other term or condition set forth in the original Service Agreement, the Assignee will receive the same services as did the Reseller and the priority of service for the Assignee will be the same as that of the Reseller. A Reseller should notify the Transmission Provider as soon as possible after any assignment or transfer of service **[30,529]** occurs but in any event, notification must be provided prior to any provision of service to the Assignee. The Assignee will be subject to all terms and conditions of this Tariff. If the Assignee requests a change in service, the reservation priority of service will be determined by the Transmission Provider pursuant to Section 13.2.

23.2 Limitations on Assignment or Transfer of Service: If the Assignee requests a change in the Point(s) of Receipt or Point(s) of Delivery, or a change in any other specifications set forth in the original Service Agreement, the Transmission Provider will consent to such change subject to the provisions of the Tariff, provided that the change will not impair the operation and reliability of the Transmission Provider's generation, transmission, or distribution systems. The Assignee shall compensate the Transmission Provider for performing any System Impact Study needed to evaluate the capability of the Transmission System to accommodate the proposed change and any additional costs resulting from such change. The Reseller shall remain liable for the performance of all obligations under the Service Agreement, except as

specifically agreed to by the Parties through an amendment to the Service Agreement.

23.3 Information on Assignment or Transfer of Service: In accordance with Section 4, Resellers may use the Transmission Provider's OASIS to post transmission capacity available for resale.

24 Metering and Power Factor Correction at Receipt and Delivery Points(s)

24.1 Transmission Customer Obligations: Unless otherwise agreed, the Transmission Customer shall be responsible for installing and maintaining compatible metering and communications equipment to accurately account for the capacity and energy being transmitted under Part II of the Tariff and to communicate the information to the Transmission Provider. Such equipment shall remain the property of the Transmission Customer.

24.2 Transmission Provider Access to Metering Data: The Transmission Provider shall have access to metering data, which may reasonably be required to facilitate measurements and billing under the Service Agreement.

24.3 Power Factor: Unless otherwise agreed, the Transmission Customer is required to maintain a power factor within the same range as the Transmission Provider pursuant to Good Utility Practices. The power factor requirements are specified in the Service Agreement where applicable.

25 *Compensation for Transmission Service*

Rates for Firm and Non-Firm Point-To-Point Transmission Service are provided in the Schedules appended to the Tariff: Firm Point-To-Point Transmission Service (Schedule 7); and Non-Firm Point-To-Point Transmission Service (Schedule 8). The Transmission Provider shall use Part II of the Tariff to make its Third-Party Sales. The Transmission Provider shall account for such use at the applicable Tariff rates, pursuant to Section 8.

26 *Stranded Cost Recovery*

The Transmission Provider may seek to recover stranded costs from the Transmission Customer pursuant to this Tariff in accordance with the terms, conditions and procedures set forth in FERC Order No. 888. However, the Transmission Provider must separately file any specific proposed stranded cost charge under Section 205 of the Federal Power Act.

27 *Compensation for New Facilities and Redispatch Costs*

Whenever a System Impact Study performed by the Transmission Provider in connection with the provision of Firm Point-To-Point Transmission Service identifies the need for new facilities, the Transmission Customer shall be responsible for such costs to the extent consistent with Commission policy. Whenever a System Impact Study performed by the Transmission Provider identifies capacity constraints that may be relieved more economically by redispatching the Transmission Provider's resources than by building new facilities or upgrading existing facilities to

eliminate such constraints, the Transmission Customer shall be responsible for the redispatch costs to the extent consistent with Commission policy.

III. Network Integration Transmission Service

Preamble

[30,530]

The Transmission Provider will provide Network Integration Transmission Service pursuant to the applicable terms and conditions contained in the Tariff and Service Agreement. Network Integration Transmission Service allows the Network Customer to integrate, economically dispatch and regulate its current and planned Network Resources to serve its Network Load in a manner comparable to that in which the Transmission Provider utilizes its Transmission System to serve its Native Load Customers. Network Integration Transmission Service also may be used by the Network Customer to deliver economy energy purchases to its Network Load from non-designated resources on an as- available basis without additional charge. Transmission service for sales to non-designated loads will be provided pursuant to the applicable terms and conditions of Part II of the Tariff.

28 *Nature of Network Integration Transmission Service*

28.1 Scope of Service: Network Integration Transmission Service is a transmission service that allows Network Customers to efficiently and economically utilize their Network Resources (as well as other non-designated generation resources) to serve their Network Load located in the Transmission Provider's Control Area and any additional

load that may be designated pursuant to Section 31.3 of the Tariff. The Network Customer taking Network Integration Transmission Service must obtain or provide Ancillary Services pursuant to Section 3.

28.2 Transmission Provider Responsibilities: The Transmission Provider will plan, construct, operate and maintain its Transmission System in accordance with Good Utility Practice in order to provide the Network Customer with Network Integration Transmission Service over the Transmission Provider's Transmission System. The Transmission Provider, on behalf of its Native Load Customers, shall be required to designate resources and loads in the same manner as any Network Customer under Part III of this Tariff. This information must be consistent with the information used by the Transmission Provider to calculate available transmission capability. The Transmission Provider shall include the Network Customer's Network Load in its Transmission System planning and shall, consistent with Good Utility Practice, endeavor to construct and place into service sufficient transmission capacity to deliver the Network Customer's Network Resources to serve its Network Load on a basis comparable to the Transmission Provider's delivery of its own generating and purchased resources to its Native Load Customers.

28.3 Network Integration Transmission Service: The Transmission Provider will provide firm transmission service over its Transmission System to the Network Customer for the delivery of capacity and energy from its designated Network Resources to service its Network Loads on a basis that is comparable to the Transmission Provider's use of the

Transmission System to reliably serve its Native Load Customers.

28.4 Secondary Service: The Network Customer may use the Transmission Provider's Transmission System to deliver energy to its Network Loads from resources that have not been designated as Network Resources. Such energy shall be transmitted, on an as-available basis, at no additional charge. Deliveries from resources other than Network Resources will have a higher priority than any Non-Firm Point-To-Point Transmission Service under Part II of the Tariff.

28.5 Real Power Losses: Real Power Losses are associated with all transmission service. The Transmission Provider is not obligated to provide Real Power Losses. The Network Customer is responsible for replacing losses associated with all transmission service as calculated by the Transmission Provider. The applicable Real Power Loss factors are as follows: [To be completed by the Transmission Provider].

28.6 Restrictions on Use of Service: The Network Customer shall not use Network Integration Transmission Service for (i) sales of capacity and energy to non-designated loads, or (ii) direct or indirect provision of transmission service by the Network Customer to third parties. All Network Customers taking Network Integration Transmission Service shall use Point-To-Point Transmission Service under Part II of the Tariff for any Third-Party Sale which requires **[30,531]** use of the Transmission Provider's Transmission System.

29 Initiating Service

29.1 Condition Precedent for Receiving Service: Subject to the terms and conditions of Part III of the Tariff, the Transmission Provider will provide Network Integration Transmission Service to any Eligible Customer, provided that (i) the Eligible Customer completes an Application for service as provided under Part III of the Tariff, (ii) the Eligible Customer and the Transmission Provider complete the technical arrangements set forth in Sections 29.3 and 29.4, (iii) the Eligible Customer executes a Service Agreement pursuant to Attachment F for service under Part III of the Tariff or requests in writing that the Transmission Provider file a proposed unexecuted Service Agreement with the Commission, and (iv) the Eligible Customer executes a Network Operating Agreement with the Transmission Provider pursuant to Attachment G.

29.2 Application Procedures: An Eligible Customer requesting service under Part III of the Tariff must submit an Application, with a deposit approximating the charge for one month of service, to the Transmission Provider as far as possible in advance of the month in which service is to commence. Unless subject to the procedures in Section 2, Completed Applications for Network Integration Transmission Service will be assigned a priority according to the date and time the Application is received, with the earliest Application receiving the highest priority. Applications should be submitted by entering the information listed below on the Transmission Provider's OASIS. Prior to implementation of the Transmission Provider's OASIS, a Completed Application may be submitted by (i) transmitting the required information to the Transmission Provider by telefax, or (ii) providing the

information by telephone over the Transmission Provider's time recorded telephone line. Each of these methods will provide a time-stamped record for establishing the service priority of the Application. A Completed Application shall provide all of the information included in 18 CFR §2.20 including but not limited to the following:

(i) The identity, address, telephone number and facsimile number of the party requesting service;

(ii) A statement that the party requesting service is, or will be upon commencement of service, an Eligible Customer under the Tariff;

(iii) A description of the Network Load at each delivery point. This description should separately identify and provide the Eligible Customer's best estimate of the total loads to be served at each transmission voltage level, and the loads to be served from each Transmission Provider substation at the same transmission voltage level. The description should include a ten (10) year forecast of summer and winter load and resource requirements beginning with the first year after the service is scheduled to commence;

(iv) The amount and location of any interruptible loads included in the Network Load. This shall include the summer and winter capacity requirements for each interruptible load (had such load not been interruptible), that portion of the load subject to interruption, the conditions under which an interruption can be implemented and any limitations on the amount and frequency of interruptions. An Eligible Customer should identify the amount of interruptible

customer load (if any) included in the 10 year load forecast provided in response to (iii) above;

(v) A description of Network Resources (current and 10-year projection), which shall include, for each Network Resource:

- Unit size and amount of capacity from that unit to be designated as Network Resource

- VAR capability (both leading and lagging) of all generators

- Operating restrictions

- Any periods of restricted operations throughout the year

- Maintenance schedules

- Minimum loading level of unit - Normal operating level of unit

- Any must-run unit designations required for system reliability or contract reasons

[30,532]

- Approximate variable generating cost ($/MWH) for redispatch computations

- Arrangements governing sale and delivery of power to third parties from generating facilities located in the

Transmission Provider Control Area, where only a portion of unit output is designated as a Network Resource

- Description of purchased power designated as a Network Resource including source of supply, Control Area location, transmission arrangements and delivery point(s) to the Transmission Provider's Transmission System;

(vi) Description of Eligible Customer's transmission system:

- Load flow and stability data, such as real and reactive parts of the load, lines, transformers, reactive devices and load type, including normal and emergency ratings of all transmission equipment in a load flow format compatible with that used by the Transmission Provider

- Operating restrictions needed for reliability

- Operating guides employed by system operators

- Contractual restrictions or committed uses of the Eligible Customer's transmission system, other than the Eligible Customer's Network Loads and Resources

- Location of Network Resources described in subsection (v) above

- 10 year projection of system expansions or upgrades

- Transmission System maps that include any proposed expansions or upgrades

- Thermal ratings of Eligible Customer's Control Area ties with other Control Areas; and

(vii) Service Commencement Date and the term of the requested Network Integration Transmission Service. The minimum term for Network Integration Transmission Service is one year.

Unless the Parties agree to a different time frame, the Transmission Provider must acknowledge the request within ten (10) days of receipt. The acknowledgement must include a date by which a response, including a Service Agreement, will be sent to the Eligible Customer. If an Application fails to meet the requirements of this section, the Transmission Provider shall notify the Eligible Customer requesting service within fifteen (15) days of receipt and specify the reasons for such failure. Wherever possible, the Transmission Provider will attempt to remedy deficiencies in the Application through informal communications with the Eligible Customer. If such efforts are unsuccessful, the Transmission Provider shall return the Application without prejudice to the Eligible Customer filing a new or revised Application that fully complies with the requirements of this section. The Eligible Customer will be assigned a new priority consistent with the date of the new or revised Application. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations.

29.3 Technical Arrangements to be Completed Prior to Commencement of Service: Network Integration Transmission Service shall not commence until the Transmission Provider and the Network Customer, or a third party, have completed installation of all equipment specified under the Network Operating Agreement consistent with Good Utility Practice and any additional requirements reasonably and consistently imposed to ensure the reliable operation of the Transmission System. The Transmission Provider shall exercise reasonable efforts, in coordination with the Network Customer, to complete such arrangements as soon as practicable taking into consideration the Service Commencement Date.

29.4 Network Customer Facilities: The provision of Network Integration Transmission Service shall be conditioned upon the Network Customer's constructing, maintaining and operating the facilities on its side of each delivery point or interconnection necessary to reliably deliver capacity and energy from the Transmission Provider's Transmission System to the Network Customer. The Network Customer shall be solely responsible for constructing or installing all facilities on the Network Customer's side of each such delivery point or interconnection.

[30,533]

29.5 Filing of Service Agreement: The Transmission Provider will file Service Agreements with the Commission in compliance with applicable Commission regulations.

30 *Network Resources*

30.1 Designation of Network Resources: Network Resources shall include all generation owned, purchased or leased by the Network Customer designated to serve Network Load under the Tariff. Network Resources may not include resources, or any portion thereof, that are committed for sale to non-designated third party load or otherwise cannot be called upon to meet the Network Customer's Network Load on a non-interruptible basis. Any owned or purchased resources that were serving the Network Customer's loads under firm agreements entered into on or before the Service Commencement Date shall initially be designated as Network Resources until the Network Customer terminates the designation of such resources.

30.2 Designation of New Network Resources: The Network Customer may designate a new Network Resource by providing the Transmission Provider with as much advance notice as practicable. A designation of a new Network Resource must be made by a request for modification of service pursuant to an Application under Section 29.

30.3 Termination of Network Resources: The Network Customer may terminate the designation of all or part of a generating resource as a Network Resource at any time but should provide notification to the Transmission Provider as soon as reasonably practicable.

30.4 Operation of Network Resources: The Network Customer shall not operate its designated Network Resources located in the Network Customer's or Transmission Provider's Control Area such that the output of those facilities

exceeds its designated Network Load, plus non-firm sales delivered pursuant to Part II of the Tariff, plus losses. This limitation shall not apply to changes in the operation of a Transmission Customer's Network Resources at the request of the Transmission Provider to respond to an emergency or other unforeseen condition which may impair or degrade the reliability of the Transmission System.

30.5 Network Customer Redispatch Obligation: As a condition to receiving Network Integration Transmission Service, the Network Customer agrees to redispatch its Network Resources as requested by the Transmission Provider pursuant to Section 33.2. To the extent practical, the redispatch of resources pursuant to this section shall be on a least cost, non-discriminatory basis between all Network Customers, and the Transmission Provider.

30.6 Transmission Arrangements for Network Resources Not Physically Interconnected With The Transmission Provider: The Network Customer shall be responsible for any arrangements necessary to deliver capacity and energy from a Network Resource not physically interconnected with the Transmission Provider's Transmission System. The Transmission Provider will undertake reasonable efforts to assist the Network Customer in obtaining such arrangements, including without limitation, providing any information or data required by such other entity pursuant to Good Utility Practice.

30.7 Limitation on Designation of Network Resources: The Network Customer must demonstrate that it owns or has committed to purchase generation pursuant to an executed contract in order to designate a generating resource

as a Network Resource. Alternatively, the Network Customer may establish that execution of a contract is contingent upon the availability of transmission service under Part III of the Tariff.

30.8 Use of Interface Capacity by the Network Customer: There is no limitation upon a Network Customer's use of the Transmission Provider's Transmission System at any particular interface to integrate the Network Customer's Network Resources (or substitute economy purchases) with its Network Loads. However, a Network Customer's use of the Transmission Provider's total interface capacity with other transmission systems may not exceed the Network Customer's Load.

30.9 Network Customer Owned Transmission Facilities: The Network **[30,534]** Customer that owns existing transmission facilities that are integrated with the Transmission Provider's Transmission System may be eligible to receive consideration either through a billing credit or some other mechanism. In order to receive such consideration the Network Customer must demonstrate that its transmission facilities are integrated into the plans or operations of the Transmission Provider to serve its power and transmission customers. For facilities constructed by the Network Customer subsequent to the Service Commencement Date under Part III of the Tariff, the Network Customer shall receive credit where such facilities are jointly planned and installed in coordination with the Transmission Provider. Calculation of the credit shall be addressed in either the Network Customer's Service Agreement or any other agreement between the Parties.

31 *Designation of Network Load*

31.1 Network Load: The Network Customer must designate the individual Network Loads on whose behalf the Transmission Provider will provide Network Integration Transmission Service. The Network Loads shall be specified in the Service Agreement.

31.2 New Network Loads Connected With the Transmission Provider: The Network Customer shall provide the Transmission Provider with as much advance notice as reasonably practicable of the designation of new Network Load that will be added to its Transmission System. A designation of new Network Load must be made through a modification of service pursuant to a new Application. The Transmission Provider will use due diligence to install any transmission facilities required to interconnect a new Network Load designated by the Network Customer. The costs of new facilities required to interconnect a new Network Load shall be determined in accordance with the procedures provided in Section 32.4 and shall be charged to the Network Customer in accordance with Commission policies.

31.3 Network Load Not Physically Interconnected with the Transmission Provider: This section applies to both initial designation pursuant to Section 31.1 and the subsequent addition of new Network Load not physically interconnected with the Transmission Provider. To the extent that the Network Customer desires to obtain transmission service for a load outside the Transmission Provider's Transmission System, the Network Customer shall have the option of (1) electing to include the entire load as Network Load for all purposes under Part III of the Tariff and designating Network

Resources in connection with such additional Network Load, or (2) excluding that entire load from its Network Load and purchasing Point-To-Point Transmission Service under Part II of the Tariff. To the extent that the Network Customer gives notice of its intent to add a new Network Load as part of its Network Load pursuant to this section the request must be made through a modification of service pursuant to a new Application.

31.4 New Interconnection Points: To the extent the Network Customer desires to add a new Delivery Point or interconnection point between the Transmission Provider's Transmission System and a Network Load, the Network Customer shall provide the Transmission Provider with as much advance notice as reasonably practicable.

31.5 Changes in Service Requests: Under no circumstances shall the Network Customer's decision to cancel or delay a requested change in Network Integration Transmission Service (*e.g.* the addition of a new Network Resource or designation of a new Network Load) in any way relieve the Network Customer of its obligation to pay the costs of transmission facilities constructed by the Transmission Provider and charged to the Network Customer as reflected in the Service Agreement. However, the Transmission Provider must treat any requested change in Network Integration Transmission Service in a non-discriminatory manner.

31.6 Annual Load and Resource Information Updates: The Network Customer shall provide the Transmission Provider with annual updates of Network Load and Network Resource forecasts consistent with those

included in its Application for Network Integration Transmission Service under Part III of the Tariff. The Network Customer **[30,535]** also shall provide the Transmission Provider with timely written notice of material changes in any other information provided in its Application relating to the Network Customer's Network Load, Network Resources, its transmission system or other aspects of its facilities or operations affecting the Transmission Provider's ability to provide reliable service.

32 *Additional Study Procedures For Network Integration Transmission Service Requests*

32.1 Notice of Need for System Impact Study: After receiving a request for service, the Transmission Provider shall determine on a non-discriminatory basis whether a System Impact Study is needed. A description of the Transmission Provider's methodology for completing a System Impact Study is provided in Attachment D. If the Transmission Provider determines that a System Impact Study is necessary to accommodate the requested service, it shall so inform the Eligible Customer, as soon as practicable. In such cases, the Transmission Provider shall within thirty (30) days of receipt of a Completed Application, tender a System Impact Study Agreement pursuant to which the Eligible Customer shall agree to reimburse the Transmission Provider for performing the required System Impact Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the System Impact Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the System Impact Study Agreement, its Application shall be deemed withdrawn and its deposit shall be returned with interest.

32.2 System Impact Study Agreement and Cost Reimbursement:

(i) The System Impact Study Agreement will clearly specify the Transmission Provider's estimate of the actual cost, and time for completion of the System Impact Study. The charge shall not exceed the actual cost of the study. In performing the System Impact Study, the Transmission Provider shall rely, to the extent reasonably practicable, on existing transmission planning studies. The Eligible Customer will not be assessed a charge for such existing studies; however, the Eligible Customer will be responsible for charges associated with any modifications to existing planning studies that are reasonably necessary to evaluate the impact of the Eligible Customer's request for service on the Transmission System.

(ii) If in response to multiple Eligible Customers requesting service in relation to the same competitive solicitation, a single System Impact Study is sufficient for the Transmission Provider to accommodate the service requests, the costs of that study shall be pro-rated among the Eligible Customers.

(iii) For System Impact Studies that the Transmission Provider conducts on its own behalf, the Transmission Provider shall record the cost of the System Impact Studies pursuant to Section 8.

32.3 System Impact Study Procedures: Upon receipt of an executed System Impact Study Agreement, the Transmission Provider will use due diligence to complete the required System Impact Study within a sixty (60) day period.

The System Impact Study shall identify any system constraints and redispatch options, additional Direct Assignment Facilities or Network Upgrades required to provide the requested service. In the event that the Transmission Provider is unable to complete the required System Impact Study within such time period, it shall so notify the Eligible Customer and provide an estimated completion date along with an explanation of the reasons why additional time is required to complete the required studies. A copy of the completed System Impact Study and related work papers shall be made available to the Eligible Customer. The Transmission Provider will use the same due diligence in completing the System Impact Study for an Eligible Customer as it uses when completing studies for itself. The Transmission Provider shall notify the Eligible Customer immediately upon completion of the System Impact Study if the Transmission System will be adequate to accommodate all or part of a request for service or that no costs are likely to be incurred for new transmission facilities or upgrades. In order for a request to **[30,536]** remain a Completed Application, within fifteen (15) days of completion of the System Impact Study the Eligible Customer must execute a Service Agreement or request the filing of an unexecuted Service Agreement, or the Application shall be deemed terminated and withdrawn.

32.4 Facilities Study Procedures: If a System Impact Study indicates that additions or upgrades to the Transmission System are needed to supply the Eligible Customer's service request, the Transmission Provider, within thirty (30) days of the completion of the System Impact Study, shall tender to the Eligible Customer a Facilities Study Agreement pursuant to which the Eligible Customer shall agree to reimburse the Transmission Provider for performing the required Facilities

Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the Facilities Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the Facilities Study Agreement, its Application shall be deemed withdrawn and its deposit shall be returned with interest. Upon receipt of an executed Facilities Study Agreement, the Transmission Provider will use due diligence to complete the required Facilities Study within a sixty (60) day period. If the Transmission Provider is unable to complete the Facilities Study in the allotted time period, the Transmission Provider shall notify the Eligible Customer and provide an estimate of the time needed to reach a final determination along with an explanation of the reasons that additional time is required to complete the study. When completed, the Facilities Study will include a good faith estimate of (i) the cost of Direct Assignment Facilities to be charged to the Eligible Customer, (ii) the Eligible Customer's appropriate share of the cost of any required Network Upgrades, and (iii) the time required to complete such construction and initiate the requested service. The Eligible Customer shall provide the Transmission Provider with a letter of credit or other reasonable form of security acceptable to the Transmission Provider equivalent to the costs of new facilities or upgrades consistent with commercial practices as established by the Uniform Commercial Code. The Eligible Customer shall have thirty (30) days to execute a Service Agreement or request the filing of an unexecuted Service Agreement and provide the required letter of credit or other form of security or the request no longer will be a Completed Application and shall be deemed terminated and withdrawn.

33 *Load Shedding and Curtailments*

33.1 Procedures: Prior to the Service Commencement Date, the Transmission Provider and the Network Customer shall establish Load Shedding and Curtailment procedures pursuant to the Network Operating Agreement with the objective of responding to contingencies on the Transmission System. The Parties will implement such programs during any period when the Transmission Provider determines that a system contingency exists and such procedures are necessary to alleviate such contingency. The Transmission Provider will notify all affected Network Customers in a timely manner of any scheduled Curtailment.

33.2 Transmission Constraints: During any period when the Transmission Provider determines that a transmission constraint exists on the Transmission System, and such constraint may impair the reliability of the Transmission Provider's system, the Transmission Provider will take whatever actions, consistent with Good Utility Practice, that are reasonably necessary to maintain the reliability of the Transmission Provider's system. To the extent the Transmission Provider determines that the reliability of the Transmission System can be maintained by redispatching resources, the Transmission Provider will initiate procedures pursuant to the Network Operating Agreement to redispatch all Network Resources and the Transmission Provider's own resources on a least-cost basis without regard to the ownership of such resources. Any redispatch under this section may not unduly discriminate between the Transmission Provider's use of the Transmission System on behalf of its Native Load Customers and any

Network Customer's use of the Transmission System to serve its designated Network Load.

[30,537]

33.3 Cost Responsibility for Relieving Transmission Constraints: Whenever the Transmission Provider implements least-cost redispatch procedures in response to a transmission constraint, the Transmission Provider and Network Customers will each bear a proportionate share of the total redispatch cost based on their respective Load Ratio Shares.

33.4 Curtailments of Scheduled Deliveries: If a transmission constraint on the Transmission Provider's Transmission System cannot be relieved through the implementation of least-cost redispatch procedures and the Transmission Provider determines that it is necessary to Curtail scheduled deliveries, the Parties shall Curtail such schedules in accordance with the Network Operating Agreement.

33.5 Allocation of Curtailments: The Transmission Provider shall, on a non-discriminatory basis, Curtail the transaction(s) that effectively relieve the constraint. However, to the extent practicable and consistent with Good Utility Practice, any Curtailment will be shared by the Transmission Provider and Network Customer in proportion to their respective Load Ratio Shares. The Transmission Provider shall not direct the Network Customer to Curtail schedules to an extent greater than the Transmission Provider would Curtail the Transmission Provider's schedules under similar circumstances.

33.6 Load Shedding: To the extent that a system contingency exists on the Transmission Provider's Transmission System and the Transmission Provider determines that it is necessary for the Transmission Provider and the Network Customer to shed load, the Parties shall shed load in accordance with previously established procedures under the Network Operating Agreement.

33.7 System Reliability: Notwithstanding any other provisions of this Tariff, the Transmission Provider reserves the right, consistent with Good Utility Practice and on a not unduly discriminatory basis, to Curtail Network Integration Transmission Service without liability on the Transmission Provider's part for the purpose of making necessary adjustments to, changes in, or repairs on its lines, substations and facilities, and in cases where the continuance of Network Integration Transmission Service would endanger persons or property. In the event of any adverse condition(s) or disturbance(s) on the Transmission Provider's Transmission System or on any other system(s) directly or indirectly interconnected with the Transmission Provider's Transmission System, the Transmission Provider, consistent with Good Utility Practice, also may Curtail Network Integration Transmission Service in order to (i) limit the extent or damage of the adverse condition(s) or disturbance(s), (ii) prevent damage to generating or transmission facilities, or (iii) expedite restoration of service. The Transmission Provider will give the Network Customer as much advance notice as is practicable in the event of such Curtailment. Any Curtailment of Network Integration Transmission Service will be not unduly discriminatory relative to the Transmission Provider's use of the Transmission System on behalf of its Native Load Customers. The Transmission Provider shall specify the rate

treatment and all related terms and conditions applicable in the event that the Network Customer fails to respond to established Load Shedding and Curtailment procedures.

34 *Rates and Charges*

The Network Customer shall pay the Transmission Provider for any Direct Assignment Facilities, Ancillary Services, and applicable study costs, consistent with Commission policy, along with the following:

34.1 Monthly Demand Charge: The Network Customer shall pay a monthly Demand Charge, which shall be determined by multiplying its Load Ratio Share times one twelfth (1/12) of the Transmission Provider's Annual Transmission Revenue Requirement specified in Schedule H.

34.2 Determination of Network Customer's Monthly Network Load: The Network Customer's monthly Network Load is its hourly load (including its designated Network Load not physically interconnected with the Transmission Provider under Section 31.3) coincident with the Transmission Provider's Monthly Transmission System Peak.

[30,538]

34.3 Determination of Transmission Provider's Monthly Transmission System Load: The Transmission Provider's monthly Transmission System load is the Transmission Provider's Monthly Transmission System Peak minus the coincident peak usage of all Firm Point-To-Point Transmission Service customers pursuant to Part II of this Tariff plus the Reserved Capacity of all Firm Point-To-Point Transmission Service customers.

34.4 Redispatch Charge: The Network Customer shall pay a Load Ratio Share of any redispatch costs allocated between the Network Customer and the Transmission Provider pursuant to Section 33. To the extent that the Transmission Provider incurs an obligation to the Network Customer for redispatch costs in accordance with Section 33, such amounts shall be credited against the Network Customer's bill for the applicable month.

34.5 Stranded Cost Recovery: The Transmission Provider may seek to recover stranded costs from the Network Customer pursuant to this Tariff in accordance with the terms, conditions and procedures set forth in FERC Order No. 888. However, the Transmission Provider must separately file any proposal to recover stranded costs under Section 205 of the Federal Power Act.

35 *Operating Arrangements*

35.1 Operation under The Network Operating Agreement: The Network Customer shall plan, construct, operate and maintain its facilities in accordance with Good Utility Practice and in conformance with the Network Operating Agreement.

35.2 Network Operating Agreement: The terms and conditions under which the Network Customer shall operate its facilities and the technical and operational matters associated with the implementation of Part III of the Tariff shall be specified in the Network Operating Agreement. The Network Operating Agreement shall provide for the Parties to (i) operate and maintain equipment necessary for integrating the Network Customer within the Transmission Provider's

Transmission System (including, but not limited to, remote terminal units, metering, communications equipment and relaying equipment), (ii) transfer data between the Transmission Provider and the Network Customer (including, but not limited to, heat rates and operational characteristics of Network Resources, generation schedules for units outside the Transmission Provider's Transmission System, interchange schedules, unit outputs for redispatch required under Section 33, voltage schedules, loss factors and other real time data), (iii) use software programs required for data links and constraint dispatching, (iv) exchange data on forecasted loads and resources necessary for long-term planning, and (v) address any other technical and operational considerations required for implementation of Part III of the Tariff, including scheduling protocols. The Network Operating Agreement will recognize that the Network Customer shall either (i) operate as a Control Area under applicable guidelines of the North American Electric Reliability Council (NERC) and the [applicable regional reliability council], (ii) satisfy its Control Area requirements, including all necessary Ancillary Services, by contracting with the Transmission Provider, or (iii) satisfy its Control Area requirements, including all necessary Ancillary Services, by contracting with another entity, consistent with Good Utility Practice, which satisfies NERC and the [applicable regional reliability council] requirements. The Transmission Provider shall not unreasonably refuse to accept contractual arrangements with another entity for Ancillary Services. The Network Operating Agreement is included in Attachment G.

35.3 Network Operating Committee: A Network Operating Committee (Committee) shall be established to coordinate operating criteria for the Parties' respective

responsibilities under the Network Operating Agreement. Each Network Customer shall be entitled to have at least one representative on the Committee. The Committee shall meet from time to time as need requires, but no less than once each calendar year.

Schedule 1--Scheduling, System Control and Dispatch Service

This service is required to schedule the movement of power through, out of, **[30,539]** within, or into a Control Area. This service can be provided only by the operator of the Control Area in which the transmission facilities used for transmission service are located. Scheduling, System Control and Dispatch Service is to be provided directly by the Transmission Provider (if the Transmission Provider is the Control Area operator) or indirectly by the Transmission Provider making arrangements with the Control Area operator that performs this service for the Transmission Provider's Transmission System. The Transmission Customer must purchase this service from the Transmission Provider or the Control Area operator. The charges for Scheduling, System Control and Dispatch Service are to be based on the rates set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 2--Reactive Supply and Voltage Control from Generation Sources Service

In order to maintain transmission voltages on the Transmission Provider's transmission facilities within acceptable limits, generation facilities under the control of the control area operator are operated to produce (or absorb) reactive power. Thus, Reactive Supply and Voltage Control from Generation Sources Service must be provided for each transaction on the Transmission Provider's transmission facilities. The amount of Reactive Supply and Voltage Control from Generation Sources Service that must be supplied with respect to the Transmission Customer's transaction will be determined based on the reactive power support necessary to maintain transmission voltages within limits that are generally accepted in the region and consistently adhered to by the Transmission Provider.

Reactive Supply and Voltage Control from Generation Sources Service is to be provided directly by the Transmission Provider (if the Transmission Provider is the Control Area operator) or indirectly by the Transmission Provider making arrangements with the Control Area operator that performs this service for the Transmission Provider's Transmission System. The Transmission Customer must purchase this service from the Transmission Provider or the Control Area operator. The charges for such service will be based on the rates set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by the Control Area operator.

Schedule 3--Regulation and Frequency Response Service

Regulation and Frequency Response Service is necessary to provide for the continuous balancing of resources (generation and interchange) with load and for maintaining scheduled Interconnection frequency at sixty cycles per second (60 Hz). Regulation and Frequency Response Service is accomplished by committing on-line generation whose output is raised or lowered (predominantly through the use of automatic generating control equipment) as necessary to follow the moment-by-moment changes in load. The obligation to maintain this balance between resources and load lies with the Transmission Provider (or the Control Area operator that performs this function for the Transmission Provider). The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Regulation and Frequency Response Service obligation. The amount of and charges for Regulation and Frequency Response Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 4--Energy Imbalance Service

Energy Imbalance Service is provided when a difference occurs between the scheduled and the actual delivery of energy to a load located within a Control Area over a single hour. The Transmission Provider must offer this

service when the **[30,540]** transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Energy Imbalance Service obligation. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

The Transmission Provider shall establish a deviation band of +/- 1.5 percent (with a minimum of 2 MW) of the scheduled transaction to be applied hourly to any energy imbalance that occurs as a result of the Transmission Customer's scheduled transaction(s). Parties should attempt to eliminate energy imbalances within the limits of the deviation band within thirty (30) days or within such other reasonable period of time as is generally accepted in the region and consistently adhered to by the Transmission Provider. If an energy imbalance is not corrected within thirty (30) days or a reasonable period of time that is generally accepted in the region and consistently adhered to by the Transmission Provider, the Transmission Customer will compensate the Transmission Provider for such service. Energy imbalances outside the deviation band will be subject to charges to be specified by the Transmission Provider. The charges for Energy Imbalance Service are set forth below.

Schedule 5--Operating Reserve - Spinning Reserve Service

Spinning Reserve Service is needed to serve load immediately in the event of a system contingency. Spinning

Reserve Service may be provided by generating units that are on-line and loaded at less than maximum output. The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Spinning Reserve Service obligation. The amount of and charges for Spinning Reserve Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 6--Operating Reserve - Supplemental Reserve Service

Supplemental Reserve Service is needed to serve load in the event of a system contingency; however, it is not available immediately to serve load but rather within a short period of time. Supplemental Reserve Service may be provided by generating units that are on-line but unloaded, by quick-start generation or by interruptible load. The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Supplemental Reserve Service obligation. The amount of and charges for Supplemental Reserve Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer

are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 7 Long-Term Firm and Short-Term Firm Point-To-Point Transmission Service

The Transmission Customer shall compensate the Transmission Provider each month for Reserved Capacity at the sum of the applicable charges set forth below:

1) Yearly delivery: one-twelfth of the demand charge of $---/KW of Reserved Capacity per year.

2) Monthly delivery: $---/KW of Reserved Capacity per month.

3) Weekly delivery: $---/KW of Reserved Capacity per week.

4) Daily delivery: $---/KW of Reserved Capacity per day.

The total demand charge in any week, pursuant to a reservation for Daily delivery, shall not exceed the rate specified in section (3) above times the highest amount in kilowatts of Reserved Capacity in any day during such week.

5) Discounts: Three principal requirements apply to discounts for transmission service as follows (1) any offer of a discount **[30,541]** made by the Transmission Provider must be announced to all Eligible Customers solely by posting on the OASIS, (2) any customer-initiated requests for discounts (including requests for use by one's wholesale merchant or an

affiliate's use) must occur solely by posting on the OASIS, and (3) once a discount is negotiated, details must be immediately posted on the OASIS. For any discount agreed upon for service on a path, from point(s) of receipt to point(s) of delivery, the Transmission Provider must offer the same discounted transmission service rate for the same time period to all Eligible Customers on all unconstrained transmission paths that go to the same point(s) of delivery on the Transmission System.

Schedule 8--Non-Firm Point-To-Point Transmission Service

The Transmission Customer shall compensate the Transmission Provider for Non-Firm Point-To-Point Transmission Service up to the sum of the applicable charges set forth below:

1) Monthly delivery: $---/KW of Reserved Capacity per month.

2) Weekly delivery: $---/KW of Reserved Capacity per week.

3) Daily delivery: $---/KW of Reserved Capacity per day.

The total demand charge in any week, pursuant to a reservation for Daily delivery, shall not exceed the rate specified in section (2) above times the highest amount in kilowatts of Reserved Capacity in any day during such week.

4) Hourly delivery: The basic charge shall be that agreed upon by the Parties at the time this service is reserved and in no event shall exceed $---/MWH. The total demand charge in any day, pursuant to a reservation for Hourly delivery, shall not exceed the rate specified in section (3) above times the highest amount in kilowatts of Reserved Capacity in any hour during such day. In addition, the total demand charge in any week, pursuant to a reservation for Hourly or Daily delivery, shall not exceed the rate specified in section (2) above times the highest amount in kilowatts of Reserved Capacity in any hour during such week.

5) Discounts: Three principal requirements apply to discounts for transmission service as follows (1) any offer of a discount made by the Transmission Provider must be announced to all Eligible Customers solely by posting on the OASIS, (2) any customer-initiated requests for discounts (including requests for use by one's wholesale merchant or an affiliate's use) must occur solely by posting on the OASIS, and (3) once a discount is negotiated, details must be immediately posted on the OASIS. For any discount agreed upon for service on a path, from point(s) of receipt to point(s) of delivery, the Transmission Provider must offer the same discounted transmission service rate for the same time period to all Eligible Customers on all unconstrained transmission paths that go to the same point(s) of delivery on the Transmission System.

Attachment A--Form Of Service Agreement For Firm Point-To-Point Transmission Service

1.0 This Service Agreement, dated as of _____, is entered into, by and between

_____ (the Transmission Provider), and _____ ("Transmission Customer").

2.0 The Transmission Customer has been determined by the Transmission Provider to have a Completed Application for Firm Point-To-Point Transmission Service under the Tariff.

3.0 The Transmission Customer has provided to the Transmission Provider an Application deposit in accordance with the provisions of Section 17.3 of the Tariff.

4.0 Service under this agreement shall commence on the later of (l) the requested service commencement date, or (2) the date on which construction of any Direct Assignment Facilities and/or Network Upgrades are completed, or (3) such other date as it is permitted to become effective by the Commission. Service under this agreement shall terminate on such date as mutually agreed upon by the parties.

5.0 The Transmission Provider agrees to provide and the Transmission Customer agrees to take and pay for Firm Point-To-Point Transmission Service in accordance with the provisions of Part II of the Tariff and this Service Agreement.

6.0 Any notice or request made to or by either Party regarding this Service Agreement shall be made to the representative of the other Party as indicated below.

[30,542]
Transmission Provider:

_____

_____

Transmission Customer:

_____
_____
_____

7.0 The Tariff is incorporated herein and made a part hereof.

IN WITNESS WHEREOF, the Parties have caused this Service Agreement to be executed by their respective authorized officials.

Transmission Provider:

By:
Name _____
Title _____
Date _____

Transmission Customer:

By:
Name _____
Title _____
Date _____

Specifications For Long-Term Firm Point-To-Point Transmission Service

1.0 Term of Transaction: _____
Start Date: _____
Termination Date: _____

2.0 Description of capacity and energy to be transmitted by Transmission Provider including the electric Control Area in which the transaction originates.

_____

3.0 Point(s) of Receipt: _____
Delivering Party: _____

4.0 Point(s) of Delivery: _____
Receiving Party: _____

5.0 Maximum amount of capacity and energy to be transmitted (Reserved Capacity): _____

6.0 Designation of party(ies) subject to reciprocal service obligation: _____

7.0 Name(s) of any Intervening Systems providing transmission service: _____

8.0 Service under this Agreement may be subject to some combination of the charges detailed below. (The appropriate charges for individual transactions will be determined in accordance with the terms and conditions of the Tariff.)

8.1 Transmission Charge: _____

8.2 System Impact and/or Facilities Study Charge(s):

_____

8.3 Direct Assignment Facilities Charge:

_____

_____

8.4 Ancillary Services Charges:

_____

_____

_____

_____

_____

_____

Attachment B--Form Of Service Agreement For Non-Firm Point-To-Point Transmission Service

1.0 This Service Agreement, dated as of _____, is entered into, by and between _____ (the Transmission Provider), and _____ (Transmission Customer).

2.0 The Transmission Customer has been determined by the Transmission Provider to be a Transmission Customer under Part II of the Tariff and has filed a Completed Application for Non-Firm Point-To-Point Transmission Service in accordance with Section 18.2 of the Tariff.

3.0 Service under this Agreement shall be provided by the Transmission Provider upon request by an authorized representative of the Transmission Customer.

4.0 The Transmission Customer agrees to supply information the Transmission Provider deems reasonably

necessary in accordance with Good Utility Practice in order for it to provide the requested service.

5.0 The Transmission Provider agrees to provide and the Transmission Customer agrees to take and pay for Non-Firm Point-To-Point Transmission Service in accordance with the provisions of Part II of the Tariff and this Service Agreement.

[30,543]

6.0 Any notice or request made to or by either Party regarding this Service Agreement shall be made to the representative of the other Party as indicated below.

Transmission Provider:

_____

_____

Transmission Customer:

_____

_____

7.0 The Tariff is incorporated herein and made a part hereof. IN WITNESS WHEREOF, the Parties have caused this Service Agreement to be executed by their respective authorized officials.

Transmission Provider:

By:
Name _____
Title _____
Date _____

Transmission Customer:

By:
Name _____
Title _____
Date _____

Attachment C--Methodology To Assess Available Transmission Capability

To be filed by the Transmission Provider

Attachment D--Methodology for Completing a System Impact Study

To be filed by the Transmission Provider

Attachment E--Index Of Point-To-Point Transmission Service Customers

_____
Customer
Date of Customer Service Agreement

_____

Attachment F--Service Agreement For Network Integration Transmission Service

To be filed by the Transmission Provider

Attachment G--Network Operating Agreement

To be filed by the Transmission Provider

Attachment H--Annual Transmission Revenue Requirement For Network Integration Transmission Service

1. The Annual Transmission Revenue Requirement for purposes of the Network Integration Transmission Service shall be _____ .

2. The amount in (1) shall be effective until amended by the Transmission Provider or modified by the Commission.

Attachment I--Index Of Network Integration Transmission Service Customers

_____
Customer
Date of Customer Service Agreement

_____

In The United States Court of Appeals
For The District of Columbia Circuit

COMPLEX
No. 97-1715

SEPTEMBER TERM, 1997

Transmission Access Policy Study Group, Petitioner	)
v.	)
Federal Energy Regulatory Commission, Respondent	)
Vermont Department of Public Service, Intervenors	)

Consolidated with Nos. 98-1111, 98-1142 and 98-1147

FINAL BRIEF FOR THE PUBLIC SERVICE COMMISSIONS OF NEW YORK, ARKANSAS AND FLORIDA, THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, THE PUBLIC UTILITY COMMISSIONS OF IDAHO, NORTH CAROLINA, AND WYOMING, THE NEW JERSEY BOARD OF PUBLIC UTILITIES, THE VIRGINIA CORPORATION COMMISSION, THE WASHINGTON

UTILITIES AND TRANSPORTATION COMMISSION, THE VERMONT DEPARTMENT OF PUBLIC SERVICE, THE NATIONAL ASSOCIATION OF UTILITY CONSUMER ADVOCATES AND THE OHIO CONSUMER COUNSEL.

[pp. 1-20]

[1]

I. STATEMENT OF THE ISSUES[2] AND STATUTORY PROVISIONS

1. Did FERC exceed its jurisdiction when it claimed authority to preempt the states' regulation of all unbundled transmission of electricity, including the unbundled intrastate transmission of electricity to retail customers?

[2]

The answer is yes.

2. Did FERC exceed its jurisdiction when it claimed authority to determine the rate treatment of all utility costs initially incurred to provide retail electric service, but subsequently "stranded" as a result of competitive access to utility systems or a municipality's formation of a public electric utility?

---

[2]This brief relies on the Petitioners' Joint Statement of the Jurisdiction and the Case for a Statement as to jurisdiction and course of proceedings as well as the statement of facts, as supplemented herein.

The answer is yes.

3. Did FERC exceed its jurisdiction when it claimed exclusive authority over regulation of facilities used in local distribution of electricity to customers who will resell the electricity to end-users?

The answer is yes.

The applicable statutes and regulations are included in a separate addendum.

II. SUPPLEMENTAL STATEMENT OF THE CASE

1. The Transmission/Distribution Distinction

The provision of electric service involves the generation of electricity and then either (i) its transmission and local distribution to the ultimate consumer (retail sale) or (ii) its transmission to a reseller (a wholesale sale), which then transmits and distributes the power to an ultimate consumer (a retail sale). Vertically integrated utilities typically generate electricity at central stations, transmit the electricity over long distances and then distribute electricity to the end-user **[3]** over local distribution lines, typically on radial systems at reduced voltages.

The key distinction between transmission facilities and local distribution facilities is that local distribution facilities normally provide one-way power to serve end-users. Power typically flows into a local distribution facility without re-entering the transmission system, i.e., power does not flow

from a local distribution system to other such systems. A transmission system usually ends at a substation where transformers reduce power voltages to lower levels for local distribution.

The bulk of a utility's system is generation and local distribution plant. Using New York as an example, approximately 15% of electric utility revenues support transmission plant; the remaining revenues support local distribution and generation plant.

2. The Wholesale/Retail Split

Traditionally, electric utilities generated, transmitted, and distributed electricity to their customers by way of their own facilities. These sales are called "bundled" sales because the customer pays a single rate for the commodity and its delivery. As indicated, utilities may also sell electricity at wholesale to another utility, which then resells the power to ultimate consumers on its facilities. Therefore, the same utility facilities are used for both wholesale and retail sales.

[4]

State commissions have traditionally regulated all aspects of bundled retail transactions, including service issues and intrastate sale and distribution of electricity.[3] Traditionally, FERC has regulated wholesale power sales and interstate transmission of electricity, which represent a small percentage of the total use of electric systems.

---

[3]The states also regulate the generation of electricity.

3. FERC'S Orders -- Matters Challenged

In the orders under review, FERC has attempted to assert jurisdiction over retail sales, when those sales are unbundled into charges for delivery and electricity. FERC concluded that "open access" gave it jurisdiction over rates for transmission of unbundled electricity for retail sales.[4] Order 888, 1991-1996 FERC Regulations and Preambles (hereinafter Stats. & Regs.) ¶31,036 at 31,980 (J.A. 349).[5] FERC also held that if a wholesale sale of energy makes use of a local distribution system, FERC acquired authority over the local distribution facilities **[5]** used for that sale. FERC Order 888-B, 81 FERC 61, 248 at 62, 098 (J.A. 1074).

Finally, FERC asserted that it has authority over "retail stranded costs," arising from a customer's choice of a new electric supplier, because of its claimed authority over unbundled retail transmission. Recognizing, however, that states had authority over the same retail stranded costs, FERC declined to exercise its purported authority. It concluded that

---

[4]FERC thus assumed that it had broader jurisdiction over the wheeling of unbundled electricity than it did over the sale of bundled electricity, and expanded its jurisdiction from 1% of utility revenues (wholesale bulk transmission) to as much as approximately 15% of total utility revenues (i.e., all transmission).

[5]FERC stated that while the states retained jurisdiction over the retail sale of the unbundled power after unbundling, it acquired jurisdiction over the unbundled transmission of that power, formerly part of the bundled retail sale. Order 888, FERC Stats. & Regs. at 31,781-82 (J.A. 150-51); Order 888-A, III FERC Stats. & Regs. ¶ 31,048 at 30,180 (J.A. 663), 30, 339-41 (J.A. 822-24).

unless the state regulatory authority lacked power under state law to address retail stranded costs there was no need for its intervention. Order 888, FERC Stats. & Regs. ¶ 31,036 at 31,825 (J.A. 194); FERC Order 888-A, III FERC Stats. & Regs. at 30,182, 30,417-419 (J.A. 898-900).

FERC further asserted jurisdiction over those utility costs that became stranded by retail customers becoming wholesale customers, for instance, through the formation of municipal electric utilities or the expansion of existing ones.[6] It reasoned such costs would not have been stranded "but for" its decision to order open access to utility transmission facilities. FERC Order 888, FERC Stats. & Regs. at 31, 818-19. FERC Order 888-A, III FERC Stats. & Regs. at 30,404. FERC stated that it would be the primary decision-maker and have the final word on **[6]** recovery of those costs. FERC Order 888-A, III FERC Stats. & Regs. at 40,405.

SUMMARY OF ARGUMENT

Congress enacted the Federal Power Act (FPA Act) in 1935 to close a gap in regulation created by a Supreme Court decision that states could not set rates for wholesale energy sold across state lines. Public Utilities Comm'n of Rhode Island v. Attleboro Steam and Electric Co., 273 U.S. 83, 89 (1927). In closing the "Attleboro Gap," Congress preserved

---

[6]An entity that had previously been served by an investor-owned electric utility could decide to municipalize, form its own municipal electric utility, become a wholesale customer, purchase bulk power from the wholesale market, and resell power to its inhabitants. In that case, certain utility costs incurred to serve the area (such as installed generating capacity) could be stranded.

the states' jurisdiction over intrastate retail transmission of electricity. In fact, the FPA expressly shielded state regulation of all retail sales and local distribution systems from FERC jurisdiction. FPA §201(b). In the Energy Policy Act of 1992 (EPAct), Congress reiterated the limitation of FERC's jurisdiction to wholesale transactions.

FERC's assertion of jurisdiction over unbundled retail transactions misreads the FPA's plain language, ignores its legislative history, and misapplies precedent.[7] FERC's attempt to regulate the rate treatment of both retail stranded costs and retail-turned-wholesale stranded costs unlawfully intrudes upon the states' exclusive jurisdiction over retail services and rates.

[7]

Finally, FERC's claim of jurisdiction over wholesale distribution ignores the language and purpose of the FPA, which preserves state authority over the transport of power on local distribution systems.

---

[7]The Federal Power Commission (FPC) acknowledged to Congress in 1947 that its jurisdiction did not include "the regulation of rates and service outside of [the Attleboro Gap]." A Bill to Amend Section 201 of the Federal Power Act, Hearings Before Subcommittee on Interstate and Foreign Commerce, 80th Cong., 1st Sess., (hereinafter "1947 Hearings"), at 506 (States' Legislative Appendix "A") . FERC's position today, however, is that the same statutory language the FPC described in 1947 as not preempting state regulation now gives FERC jurisdiction over the transmission of electricity to retail customers.

FERC's position is shown in Attachment A. The States' position is reflected in Attachment B.

POINT I[8]

CONGRESS PRESERVED THE STATES' LONGSTANDING JURISDICTION OVER THE REGULATION OF INTRASTATE RETAIL TRANSMISSION

The Act does not define "transmission" for retail purposes, presumably because customers in 1935 did not pay separate rates for the generation, transmission and distribution of electricity. A full reading of the Act, however, together with its legislative history and the Attleboro case that engendered it, shows that the 1935 Congress preserved the states' longstanding authority over retail intrastate service. Such a reading shows Congress intended that: (1) the regulation of retail transactions be left with the states (1947 Hearings at 547-548) ; and (2) that all solely intrastate transactions be subject to state, not federal, jurisdiction.

[8]

A. In Filling The Attleboro Gap, Congress Did Not Diminish The States' Jurisdiction Over Retail Transactions

---

[8]The Arkansas Public Service Commission does not join in this point.

1. Congress Reserved To The States Jurisdiction Over Intrastate Service

Under Section 201(a), 16 U.S.C. § 824(a), FERC may regulate the transmission of electric energy only if the energy is "consumed," or used, in a state other than that in which it was initially transmitted, and if the transmission, is not "subject to regulation by the States."[9] Notwithstanding this statutory constraint, FERC has concluded that "open access" would give it jurisdiction over the transmission of unbundled electricity for retail sales.[10] FERC Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,966 (J.A. 335). FERC's attempt to regulate the transmission of energy for all unbundled retail sales conflicts with the express limitation of FERC's authority. Under the FPA, the states have regulated the transmission of retail energy sales for over 60 years.

---

[9]The Act applies to transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce . . . . such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States," 16 U.S.C. §824(a) (emphasis added). "Electric energy shall be held to be transmitted in interstate commerce if transmitted from a state and consumed at any point outside thereof . . ." 16 U.S.C. §824(a) .

[10]FERC has thus assumed that it has broader jurisdiction over the wheeling of unbundled electricity than it had over the sale of bundled electricity, and has expanded its jurisdiction from 1% of utility revenues (wholesale bulk transmission) to as much as approximately 15% of total utility revenues (i.e., all transmission).

[9]

FERC argues that its limited jurisdiction over the transmission of certain electricity encompasses retail transactions because Congress did not expressly limit its jurisdiction to wholesale transmissions. Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,966-67 (J.A. 335-36). Given that "the existence of federal authority to act should appear affirmatively and not rest on inference alone" (Connecticut Light & Power v. Fed. Power Comm'n, 324 U.S. 515, 532 (1945), quoting Yonkers v. U.S., 320 U.S. 685, 692 (1944)), and FERC's inference countermands the Act's safeguarding of state jurisdiction over "local distribution" and facilities used "only for the transmission of electric energy in intrastate commerce," (16 U.S.C. § 824(b)), Order 888 thereby violates the Act's plain language.[11] See Cities of Batavia, Naperville, Rock Falls et al. v. F.E.R.C., 672 F.2d 64, 68, n.2 (D.C. Cir. 1982) [wherein this Court upheld FERC's decision that it lacked jurisdiction over retail rates under 16 U.S.C. section 824j].[12]

---

[11]"(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but . . . shall not apply to any other sale of electric energy . . ." 16 U.S.C. section 824(b) (emphasis added).

[12]In 1935, most electric facilities were intrastate facilities (Hearings on H.R. 5423, House Committee on Interstate and Foreign Commerce, 74th Cong., 1st Sess., [hereafter "1935 Hearings"] at 413 and 763). Thus, states' rights advocates in Congress added the "intrastate" clause to the FPA "so that [the Act] specifically will not apply to intrastate business." New York Times,

[10]

2. The Courts and FERC. Itself Have Recognized That Congress' Goal Was To Fill The "Attleboro GAD" Which Had Left Wholesale Transmission Unregulated

The genesis of the Federal Power Act was the Supreme Court decision in Attleboro that state regulation of interstate wholesale sales would burden interstate commerce. 273 U.S. at 89. In the absence of federal regulation, however, that decision meant no regulation of interstate sales whatsoever. Congress filled this "Attleboro Gap" by empowering the FPC to regulate wholesale electricity rates.[13]

June 8, 1935, "Utility Foes Map Floor Fight, 1935 Hearings, Testimony of John E. Benton, General Sollcitor, NARUC, at 748, 763 et seq.

[13]Dozier DeVane, Solicitor of the Federal Power Commission, stated to the House Committee on Interstate and Foreign Commerce that: "... [S]ection 201 is intended to give the Federal Power Commission jurisdiction over the wholesale rates only. (1935 Hearings at 497) ... [T]he plan of this bill with reference to the regulation of rates [is that] it seeks to leave in the state commissions the power to regulate retail rates but through some federal agency assist the state commissions making available to them the proper data for the determination of those rates. Id. at 520. To the same effect, H.R. Report No. 1318, 74th Cong., 1st Sess., at 8, "the [Federal Power] Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce" (emphasis added).

But the Act was not a preemption statute; indeed, it preserved state authority in retail matters. The Supreme Court has emphasized that the specific language of FPA section 201(b) expressed Congress' intent to draw a "bright line" easily ascertainable between state and federal jurisdiction:

> What Congress did was to adopt the test developed in the Attleboro line which denied state power to regulate a sale 'at wholesale to local distributing companies' and allowed state regulation of a sale 'at local retail rates to ultimate consumers.' [citation omitted].

[11]

This conclusion has been consistently reaffirmed in subsequent cases. In Panhandle Eastern Pipeline Co. v. Public Service Commission of Ind., 332 U.S. 507, which considered the reach of §l(b) of the Natural Gas Act, the Court said that 'the line of the statute was thus clear and complete. It cut sharply and cleanly between sales for resale and direct sales for consumptive uses. No exceptions were made in either category for particular uses, quantities or otherwise.'

Fed. Power Comm'n v. Southern California Edison, 376 U.S 205, 214, 215 (1964), citations omitted (emphasis added). In the ensuing years, the states have regulated all aspects of electric service to retail customers, as Congress intended.

FERC based its claim here to preempt state regulation of transmission to retail customers on Fed. Power Comm'n v. Florida Power & Light, 404 U.S. 453 (1972), reh'g denied, 405 U.S. 948 and Jersey Central Power & Liqht v. Federal Power Comm'n, 319 U.S 61(1943). Those cases, however,

were "purely factual" disputes (Florida Power & Light at 463)[14] and uphold FERC's accounting authority over public utilities connected to an interstate grid. Indeed FERC's brief to the Supreme Court expressly disavowed any intention to seek jurisdiction over retail sales. As FERC (FPC) stressed:

> [F]inally, and most important, the Commission's rate jurisdiction over interstate **[12]** sales was limited to sales at wholesale; no authority over retail sales was granted.

FPC Brief on Writ of Certiori to the U.S. Supreme Court, October Term, 1970 at 20, 21 (emphasis added); see FPC v. Southern Cal. Edison, 376 U.S. 205, supra. Thus, FERC cannot now point to Florida Power & Light and Jersey Central as a basis for preempting state jurisdiction over retail transmission.

FERC's position here also conflicts with its longstanding view that the FPA need not be amended to clarify its protection of State authority. In 1947, the FPC stated "in the regulation of rates and service, the definitions [in the Act] have been so drawn to plug and no more the Attleboro gap." 1947 Hearings at 527. And in response to an amendment, proposed in 1967, after the 5th Circuit's decision in Florida Power & Light (discussed supra), the FPC testified that such an amendment was "unwarranted" because "the

[14]See Carstens, Friends of the Earth, et al. v. N.R.C., 742 F.2d 1546, 1557 (D.C. Cir. 1984) [citing Florida Power & Light for the proposition that when a court considers "a purely factual question within [its] area of competence" the court should defer to the agency.") The issue here is a question of law.

accounting situation (such as the one in Florida Power & Light) differs from rate jurisdiction, where the states regulate retail sales and the FPC regulates wholesales" See 1967 Hearings, Testimony of Hon. Lee C. White, Chairman, Federal Power Commission, at 121, 123, 125.[15]

[13]

3. In 1992 Congress Reiterated That States Would Regulate All Retail Deliveries of Electricity

While expanding FERC's authority to order wholesale wheeling, Congress in 1992 reiterated that FERC could not preempt state regulation of retail wheeling of electricity. 16 U.S.C. §824k. EPAct states: "Nothing in this subsection [giving FERC authority over wholesale wheeling] shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an

[15]Notwithstanding its prior assurances to Congress, FERC Order 888 states that "to the extent that retail wheeling involves transmission in interstate commerce by public utilities, the rates, terms and conditions of such service are subject to the exclusive jurisdiction of the Commission" (Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,966 (J.A. 335)).

ultimate consumer" 16 U.S.C. §824k(h) (emphasis added).[16] The legislative history confirms that:

> "the vast majority of the activities of the electric utility industry are subject to state public utility commission jurisdiction, and that has not been changed by this legislation, . . . (Congressional Record, October 8, 1992, at S. 34013). This [act] manifests Congressional intent to continue to limit the FERC's authority to wholesale transactions only, Id. at 34015 (emphasis added) . . . the FERC's authority is strictly limited to transmission services provided for the delivery of bulk power supplies to legitimate wholesale customers" Id. at 34018 (emphasis added).

(emphasis added).

FERC Order 888 misreads EPAct as merely prohibiting FERC from ordering retail wheeling, impliedly assigning FERC jurisdiction over retail wheeling rates. There is no language in **[14]** EPAct that even remotely suggests that although Congress prohibited FERC from ordering retail wheeling, it intended FERC to preempt the states' jurisdiction over retail wheeling rates contrary to FERC's conclusion in

---

[16]EPAct should, of course, be read in concert with the 1935 Act. See Imazio Nursery, Inc. v. Greenhouses, 69 F.3d 1560, 1564 (Fed. Cir. 1995) ["It is an elementary rule of construction that all parts of an act relating to the same subject should be considered together . . ."].

Order 888, FERC Stats. & Regs. at 31,781 (J.A. 150). Rather, EPAct gave FERC jurisdiction to order wholesale wheeling on a case-by-case basis, and preserved the states' authority over retail transactions.[17]

4. The Unbundling Of Transmission Rates Does Not Transfer The States' Jurisdiction Over Intrastate Retail Sales To FERC

Nothing in the FPA or its legislative history implies that unbundling a retail sale would exclude the intrastate transportation component of that sale from state jurisdiction, leaving the states with control over only the commodity. The underlying transaction remains an intrastate transmission of energy to retail customers, which is the part of the transaction directly affecting customers that Congress left with the states. 16 U.S.C. §824(b)-(c) . See Arkansas Elec. Coop. Corp. v. Arkansas Public Service Comm'n, 461 U.S. 375, 394 (1983)

---

[17]FERC stated that its primary purpose for issuing FERC Order 888 and its progeny is "to remedy undue discrimination in the provision of interstate transmission services by public utilities." FERC Order 888-A, III FERC Stats. & Regs. at 30,175 (J.A. 658) . It presents no evidence, however, that discrimination has taken place, and it has not even attempted to show why state commissions are incapable of preventing such discrimination at the retail level. See Congressional Record, October 8, 1992, Discussion of Senator Wallop (R-Wy), at S. 34014. FERC can address alleged discriminatory denial of transmission access in wholesale sales or in wholesale transmission rates sales. FERC's dramatic seizure of power over unbundled retail transmission, however, is not supported by any Congressional goal of preventing discrimination.

[15] [["a]lthough AECC is tied into an interstate grid, its basic operation consists of supplying power from generating facilities located within the State to member cooperatives, all of which are located within the State"].

FERC's reading of the EPAct, if adopted, would also impede Congress' goal of encouraging competition in the electricity market. See Energy Policy Act of 1992, Pub. L. No. 102-486, 1992 U.S.C.C.A.N (102 Stat.) 1961-1962. Under FERC's theory, states that advanced Congress' will by unbundling retail tariffs would suffer diminished jurisdiction, while states that did not unbundle, and thereby impeded competition, would avoid preemption.[18]

United Distribution Companies v. Federal Energy Regulatory Comm'n, 88 F.3d 1105, 1153 (1996), cert. denied, 117 S. Ct. 1723 (1997), cited by FERC to support its contrary claim (FERC Order 888-A, III FERC Stats. & Regs.

---

[18]FERC's decision on retail transmission gives rise to a variety of transmission arrangements. For instance, (1) an end-user could choose bundled service, which FERC agrees is fully subject to state regulation; or (2) an end-user could purchase electricity from a "reseller" of energy that is the wholesale customer for the unbundled transmission service; finally, (3) an end-user could piece together its own package of services by purchasing unbundled transmission service from a utility and purchasing energy from a wholesaler, either from out-of-state (3a), where it would be an unbundled retail transmission in interstate commerce, or in-state (3b) when it would be an unbundled retail transmission in intrastate commerce.

at 30,336 (J.A. 819), does not do so. Among other distinctions, United Distribution addressed only interstate gas transportation. 88 F.3d at 1153. ["FERC retains jurisdiction over the interstate transmission component of a retail sale" (emphasis added)]. Indeed, this Court **[16]** distinguished its holding giving FERC jurisdiction over interstate transportation from those "interstate pipelines that receive natural gas at their state boundary that is consumed within the state and subject to state commission regulation." United Distribution, 88 F.3d at 1153, n.62.

5. FERC's Jurisdictional Arguments Do Not Warrant Deference

Because Congress has spoken directly to the matter at issue, FERC's construction of its statute is entitled to no special deference:

> If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency must give effect to the unambiguously expressed intent of Congress. Chevron U.S.A.v. Natural Resources Defense Council, Inc., 467 U.S. 837, 842-43 (1984).

In sections 201(a), 201(b) and 212(h) of the Federal Power Act, Congress preserved state power over retail sales. Moreover, defining retail jurisdiction does not require application of FERC's technical expertise (Compare, Elec. Indus. Ass'n Consumer Elecs. Group v. FCC, 636 F.2d 689, 695 (D.C. Cir. 1980)); nor do the general provisions of the FPA delegate to FERC oversight over the complexities of the

entire electric industry (Compare, Dept of Health and Human Services v. Fed. Labor Relations Auth., 976 F.2d 1049 (D.C. Cir. 1992)).

Even if Congressional intent were unclear, FERC's construction would not deserve deference because, where a federal agency attempts to preempt areas traditionally regulated by the **[17]** states, the Court "start[s] with the assumption that the historic police powers of the States were not to be superseded unless that was the clear and manifest purpose of Congress." Hillsborough County v. Automated Medical Laboratories, Inc., 105 S. Ct. 2371, 2376 (1985).

Further, FERC's assertion of jurisdiction over retail transmission is unsupported by statutory language or history, which abound in contrary statements. Chevron U.S.A.v. Natural Resources Defense Council, Inc., 467 U.S. 843 (1984); Southeastern Michigan Gas Co. v. FERC, 133 F.3d 34, 43 (D.C. Cir. 1998). The FPC itself stated that: "The important task of the regulation of consumers' rates is left entirely to the States. 1935 Hearings, Testimony of FPC Commissioner Clyde Seavey at 384 (emphasis added); see New York Times, March 8, 1935, "Rayburn Bill Held No Blow To States". Although Congress, in 1935, could not contemplate a competitive, unbundled market, it clearly relied on the FPA's precise assignment of state jurisdiction, which "carefully preserved the States' essential regulatory authority over matters of local import," and did "not assign to the Commission any authority over retail rates." 1967 Hearings at 124 (emphasis added).

B. FERC Regulation of Intrastate Retail Transmission Would Be Unwieldy And Detrimental To Electric Customers

1. FERC Regulation Would Be Infeasible

Ratemaking entails a delicate balancing of interests (e.g., Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989)), particularly with respect to retail rate regulation, which **[18]** involves numerous, diverse customers. When asked in 1947 whether the federal government was better equipped than the states to regulate retail rates and services the FPC's Assistant General Counsel stated, "I definitely say, No" (1947 Hearings at 575). single federal agency simply cannot balance ratepayer and shareholder interests for hundreds of companies nationwide.

2. The States Are Better Equipped To Regulate Customer Service

The development and enforcement of retail service standards also requires sensitivity to local conditions that only state commissions can provide. Overly stringent standards can drive up costs and deter economic growth, while insufficient safeguards can endanger customers' safety and welfare.[19]

---

[19]For example, FERC has made it clear that it does not intend to apply gross negligence standards commonly applied by states in assessing a utility's liability for service failures. American Elec. Power Serv. Corp. et al, 78 F.E.R.C. ¶61,070 at n. 28 (1997); New York State Elec. & Gas Corp., 79 F.E.R.C. ¶61,371

Under FERC's approach, it would be required to handle retail customer complaints about transmission service from all over the country. The States are in a far superior position to handle customer service problems and protect the rights of small retail consumers.

Beyond that, the advent of retail access enables millions of retail electric customers to contract with alternative **[19]** providers of transmission service. Inevitably, these customers will encounter service, billing and other difficulties. State organizations that have long dealt with similar problems will be able to deal with those issues when they arise in an unbundled environment. FERC lacks any capability to handle complaints of retail customers, yet its approach would require it to do just that.

3. FERC Preemption Could Undermine The Reliability Of Electric Service

Reliability standards for electric service, and the costs that should be incurred to meet them, must be addressed on a local level based on local system conditions. These issues defy a one-size-fits-all analysis.

(1997), 1997 FERC Lexis 1244 at 16, n.15. These state "gross negligence" standards have been upheld by state courts (see, e.g., Food Pageant v. Consolidated Edison Co., 54 N.Y.2d 167, 172 (1981); San Diego Gas & Elec. Co. v. Superior Ct. of Orange County, 13 Cal. 4th 893, 917 (1996); Garrison v. Pacific Northwestern, 45 Ore. App. 523, 526 (1980)). Holding utilities to an ordinary negligence standard could raise their costs dramatically, a trade-off best assessed by state agencies.

Additionally, FERC's open access provisions conflict with state provisions for energy balancing, dispute resolution, customer security deposit requirements, consumer complaints, and credit worthiness requirements for receiving service. See, Consolidated Edison Co. of N.Y., Open Access Transmission Tariff, Docket No. ER98-1631-000 and ER 98-270-000 [wherein Con Edison has requested waivers from FERC for such requirements]. While FERC has deferred to the states on some of these issues, it nonetheless claims the last word on various intrastate matters reserved by Congress to the states. Additionally, FERC's Open Access provisions cannot realistically be applied to retail service, so utilities and state commissions have been forced to seek FERC waivers on a variety of issues pertaining to retail access.

[20]

The states have more of the information needed to determine the level of reliability required to maintain customer satisfaction and economic health and to respond to system emergencies. It is not feasible for a federal agency to become familiar with the intricacies of local system design and the needs of the many disparate areas within each of the contiguous 48 states. The tendency to develop a one-size-fits-all approach based solely on national goals could be ruinous to local service reliability.

* * * * *

[pp. 30-32]

[30]

B. FERC's Theory For Preempting State Jurisdiction Over Local Distribution Facilities Is Baseless

1. FERC's Theory Conflicts With Its Identification Of Facilities As Local Distribution

FERC created a jurisdictional test consisting of seven indicators to be applied in determining whether a facility is "local distribution," and hence beyond its jurisdiction.[33] If FERC's criteria establish that a facility is a local distribution facility, then the facility and the transport of energy on it are exempt from FERC's jurisdiction as a matter of law, even though the transactions occurring on it are wholesale transactions.

Case law (as FERC itself recognized in Order 888)[34] exempts local distribution facilities from federal jurisdiction and requires that before FERC can assert jurisdiction over such facilities, it must first make a factual determination that they are not local distribution facilities.

---

[33]FERC Order 888, FERC Stats. & Regs. at 31,770-71 (J.A. 139-40), 31,780-83 (J.A. 149-52) .

[34]FERC Order 888, FERC Stats. & Regs. at 31,783, n. 546 (J.A. 152).

> Whether facilities are used in local distribution -- although a limitation on FPC jurisdiction and a legal standard that must be given effect in addition to the technological transmission test (citation omitted) -involves a question of fact to be decided by the FPC as an original matter. Federal Power [31] Commission v. Southern California Edison Co., 376 U.S. 205, at 210, n.6 (1964).

This holding, by which FERC itself was "particularly persuaded,"[35] makes no distinction between bundled and unbundled sales. The seven-indicator test established in FERC Order 888[36] represents FERC's current judgment as to what constitutes local distribution, and should be applied in all instances to define the local distribution facilities subject to state regulation rather than federal.[37]

---

[35]Order 888, FERC Stats. & Regs. at 31,783 (J.A. 152), n. 546.

[36]FERC Order 888, FERC Stats. & Regs. at 31,770-71 (J.A. 139-40), 31,780-83 (J.A. 149-52).

[37]In Connecticut Power & Light v. Federal Power Comm'n, 324 U.S. 515 (1945), the Court first expressed the need to limit the corresponding potential reach of federal jurisdiction and then discussed the need for enforcing the local distribution facilities exemption in order to reconcile the claims of federal and local governments.

In Arkansas Power & Light v. Federal Power Comm'n, 368 F.2d 376 (8th Cir. 1966), the Commission argued that

FERC ignores its own factual determination when it claims jurisdiction over any facility transporting energy for **[32]** resale.[38] It apparently reasoned that, because wholesale sales of energy, by definition, do not occur on local distribution facilities, such sales must therefore transform a facility that would otherwise be "local distribution" into a FERC-jurisdictional facility. This reasoning is illogical, however; clearly, the function of a facility does not depend on whether a wholesaler decides that title to energy will pass to

---

inasmuch as there were wholesale sales for resale, the nature of the lines was irrelevant. The Court noted that, although the Commission stated that evidence concerning the nature of the lines was not relevant, it had made a factual finding as to local distribution and thereby complied with Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205, at 210 n. 6, infra.

[38]FERC cites Wisconsin-Michigan Power Co. v. Federal Power Comm'n, 197 F.2d 472 (7th Cir. 1952), in its discussion of jurisdiction over wholesale distribution. Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,914 (J.A. 283). That case, however, stands for the proposition that FERC lacks jurisdiction over facilities that it finds to be "local distribution." The Court determined that sales to wholesalers for resale were not made over facilities used in local distribution because the facilities employed were not located at points on the system where local distribution starts and is carried. The court noted that jurisdiction over local distribution of electric energy is reserved to the states and the authority of the states to fix local rates is not disturbed, even in those cases where the energy is brought in from another state. 197 F.2d at 476.

a reseller at a retail customer's meter or path at some upstream point, such as a utility substation.

FERC offers no reasoned analysis of why local distribution should be defined differently for wholesale sales and retail sales; its decision to attempt such a differentiation without such analysis and explanation should be rejected as arbitrary. Transactive Corp. v. United States, 91 F.3d 232 (D.C. Cir. 1996).

EPRI PRIMER ON ELECTRIC POWER FLOW FOR ECONOMISTS AND UTILITY PLANNERS

[February 1995]

[p. 1]

EPRI
Electric Power
Research Institute

Keywords:
Electric circuits
Optimal power flow
Economic analysis
Marginal costs
Transmission costs

EPRI TR-104604
Project 2123-19
Final Report
February 1995

A Primer on Electric Power Flow for Economists and Utility Planners

Prepared by
Incentives Research Inc.
Boston, Massachusetts

* * * * *

[2-6]
Resistance and Ohm's Law

Since power is dissipated in a circuit, some force that is opposed to the flow of current must be at work. The example of a locomotive is analogous in some respects. In a frictionless, gravitation-free world, once the initial inertia had been overcome and the locomotive had been given momentum, the locomotive would continue indefinitely its motion at a constant speed without further work being required. But in the real world, power must be applied continually to compensate for frictional forces opposing the direction of motion in order to maintain the locomotive's speed.

A similar problem arises within a conductor. The electrical analogue to file coefficient of friction is *resistance* (symbol *R)*. The resistance of a conductor is a measure of its opposition to current flow; it is a physical property that varies with the conductor's shape, temperature, and other factors. The unit of resistance is the *ohm* (usually signified by the upper case Greek letter omega, Ω).[8] Certain resistance in a conductor can be understood by regarding resistance as being file result of electron-atom "collisions" within the conductor.[9]

---

[8]Named for German physicist George Simon Ohm (1787-1854).

[9]Technically, the electrons and conductor atoms do not collide like billard balls, but the movement of the electrons is deflected in a fashion similar to collisions by the electrical fields

When current flow is increased, more collisions occur and more power is dissipated. The resistance of a copper wire is halved when its cross-sectional area is doubled because fewer electron-atom collisions will occur in a thicker wire. A wire with twice the length will also have twice as many collisions and therefore twice the resistance.

> A good conductor allows electrons to flow easily, but they do not necessarily flow fast. The average electron drift velocity is equal to the current per cross-sectional area of a wire divided by the electron density. Algebraically: $v = i/(Ad)$. Applying this formula we discover, perhaps **[2-7]** surprisingly, that the speed of electrons in a current-carrying conductor is very low. In copper there are roughly 1.38×1024 free electrons per cubic inch; a #14 AWG copper wire (which is about 1/16 inch in diameter) has a cross-sectional area of 3.23×10^{3} square inches. For a current of ten Amperes the electron drift velocity is only v = 0.000356 meters per second, or 1.28 meters per hour![10] Of course, an immense nmnber of electrons is moving at this lethargic pace. Moreover, the electric impulses (voltage propagation) associated with these electron movements travel at nearly the speed of light,

surrounding the electrons of the conductor atoms.

[10] 1.28 m/h = [10C/s]·[1/3.238x10^{-3} in^2]·[1in^{3}1.38x10^{24}electrons]·[0.254m/inch]·[1 electron/1.602x10^{-19}C]

> $c = 2.978 \times 10^{8}$ meters per second. Each electron's movement induces a sequence of movements in other electrons downstream in the wire, with the result being current (or power) that propagates at an enormous speed.

Good conductors have small values for R. A measure of the lack of opposition to current in a conductor, *conductance,* is the reciprocal of the resistance of the conductor: $G = 1/R$. The SI unit of conductance (G) is the *siemens* (S) or the mho.[11]

A *resistor* is a circuit element flint has a known resistance. Electronic circuits often include numerous resistors of different sizes. Their combined effect can be determined using the following rules of combination for resistors:

[Diagram omitted]

The effective resistance of n resistors in *series* (placed sequentially in a single path) is the sum of their individual resistances:

$$R_{total} = R_1 + R_2 + \ldots + R_n.$$

[Diagram omitted]

[11] The siemens is named for British engineer Sir William Siemens (1823-1883).

The effective conductance of *n* resistors in *parallel* (placed side by side, creating alternative paths) is the sum of their individual conductances:

$$G_{total} = G_1 + G_2 + \ldots + G_n,$$

or equivalently,

$$1/R_{total} = 1/R_1 + 1/R_2 + \ldots +$$

Note that this R_{total} will be smaller than any of the individual parallel resistances.

Individual conductors have a fairly constant resistance under normal operating conditions.[12]

[Diagram omitted]

[2-8]

Ohm's Law states that the current through a conductor is directly proportional to the applied voltage, where the proportionality constant is the conductance of that conductor: $I = EG = E/R$. One ohm is defined as the resistance that permits a current of one ampere to flow when a potential difference of one volt is applied across the resistance: 1Ω=(1 V)/1 Λ. One way to think of resistance, current, and voltage is to compare a resistor to a hole in a leaky balloon. The air

[12]For the purposes of this chapter, conductors will be treated as idealized, having no resistance, while circuit elements will be treated as having a constant *R* that does not vary with conditions of use. In practice, temperature can affect the resistance of both conductors and electronic components.

in a balloon will escape faster (increased current) if the hole is widened (reduced resistance). Another way to increase the rate of escape is to increase the pressure differential (increased voltage) between the gas inside the balloon and the gas outside the balloon.

As stated previously, voltage is the ratio of power to current ($E = P/I$). Multiplying both sides of this equation by I yields $P = EI$, so the power dissipated by a circuit is the product of the voltage and the current. Substituting $I = E/R$ from Ohm's Law into the power equation shows that $P = E \cdot (E/R) = E^2/R$. Alternatively, substitution of Ohm's Law in the form $E = IR$ yields $P = IR \cdot I = I^2R$. Thus for a circuit with resistance R, power dissipation increases as the square of voltage or current, e.g. doubling file applied voltage doubles the current but quadruples the power dissipation.

The above rules on combining resistances imply that if a voltage is applied to resistors in series, the current through each of the resistors will be the same, $I = E/R_{total}$. If the resistors are in parallel, each resistor of a different size will have its own corresponding current, but the total current will be $I_{total} = E \cdot G_{total}$

Kirchhoff's Laws

Almost any interesting circuit consists of several paths serving several kinds of devices. Kirchoff's Laws define physical constraints governing how power or current will flow in any network with several paths:

- *Kirchhoff's Current Law* (KCL) states that the sum of the currents entering a point in an electric circuit must

equal the sum of the currents leaving that point. Equivalently, the net current into and out of any point must be zero.

[2-9]

- *Kirchhoff's Voltage Law* (KVL) states that in any closed electric circuit, the sum of the voltage drops across the circuit elements must equal the sum of the applied emf's around every closed loop.

With the use of these laws, the flows on a simple circuit can be predicted. The circuit at right [diagram omitted] includes a direct voltage source (12 V battery), a resistive load (a lamp rated 3 W at 12 V), a switch, and a few conductors (wires) linking these components in series. The resistance of the wires and internal resistance of the battery can be ignored since they are very small compared to the resistance of the lamp.

When the switch is open, there is no path through which the current may flow. Closing the switch creates a path. KVL states that the net voltage around the closed loop must be zero. Since the battery is providing 12 volts, the *voltage drop* across the resistor must also be 12 volts. That is, the potential difference between points A and B is 12 V, but between B and C it is zero. The amount of current that flows can be determined with the voltage-defining equation E = P/I. The lamp draws 3 W at 12 V, so the current flow

$$I = P/E = (3\text{W})/(12\text{ V}) = 0.25\text{ A}.$$

The lamp is a special kind of resistor, the resistance of which can be deduced from Ohm's Law:

$$R = E/I = (12\text{ V})/(0.25\text{ A}) = 48\Omega.$$

Adding another 48Ω lamp in series to the existing circuit elements will alter the circuit in several respects. The direct voltage source still provides 12 V, but the total resistance is doubled, to 96 Ω, since series resistance is additive. The entire supply current flows through both of the resistors (lamps) but is now smaller:

[Diagram omitted]

$$I = E/R_{total} = (12\text{ V})/(96\ \Omega) = 0.125\text{ A}.$$

The voltage (drop) across the original lamp is now half as large:

$$E = IR = (0.125\text{ A})(48\ \Omega) = 6\text{ V}.$$

[2-10]

We could have used Kirchoff's Laws to establish these results: By KVL, the voltage drop across the two lamps must add up to 12 volts. Since the two have the same resistance value, the voltage drop across each must be the same, i.e. 6 volts. By KCL, the current flowing in the loop must be the same as the current flying across each resistor:

$$I = E/R = (6\text{ V})/(48\ \Omega) = 0.125\text{ A}$$

Total power dissipated with two lamps in series is:

$$P = EI = (12\ \text{V})(0.125\ \text{A}) = 1.5\ \text{W},$$

versus 3 W with only one lamp. Thus less light is enjoyed than would have been produced by one lamp alone.

[Diagram omitted]

Placing the second 48 Ω lamp in parallel instead of in series produces a different result. Total conductance is additive for parallel resistors, so

$$\begin{aligned} G_{total} &= 1/(1/R_1 + 1/R_2) \\ &= 1/(1/48 + 1/48) = 1/24 \text{ siemens} \end{aligned}$$

The effective resistance of the two lamps in combination is therefore

$$R_{total} = 1/G_{total} = 24\ \Omega,$$

one-half of the resistance of either lamp by itself. By KVL, the voltage across each lamp is the same and equal to the source emf, 12 V, so the current through the original lamp is

$$I_1 = E \bullet G_1 = 12\ \text{V})/(48\ \Omega) = 0.25\text{A}.$$

Since G_2 is the same as G_1, I_2 also equal 0.25 A. By KCL the total current supplied by the battery is:

$$I = I_1 + I_2 = 0.25\ \text{A} + 0.25\ \text{A} = 0.5\ \text{A}.$$

Total power dissipation in the form of light is now $P = E/=$ (12 V)(0.5 A) = 6 W, twice as much as with one lamp alone (so now our battery will not last as long).

Thus we see that the number and location of circuit elements has a critical effect on the currents, voltages, and power dissipation in the circuit. In this example, adding the second lamp will either halve or double the total power dissipation in the circuit, depending on whether the new lamp is installed in series or parallel. Accordingly, for any planned circuit, the designer must anticipate that both of Kircboff's Laws will hold when choosing the location of circuit elements.

KCL is true because electrons are never destroyed or created at any point in the circuit. KVL is a consequence of the fact that current always flows through a circuit in a fashion **[2-11]** that minimizes power consumption (I^2R losses). To demonstrate this connection to minimal power losses, consider the following circuit:

Power dissipation $\begin{aligned} P &= I_1^2R_1 + I_2^2R_2 \\ &= I_1^2R_1 + (I - I_1)^2 R^2 \\ &= I_1^2R_1 + I^2R_2 - 2II_1R_2 + I_1^2R_2 \end{aligned}$

P is now a function of I_1 having a minimum where

$$dP/dI_1 = 2I_1R_1 - 2IR_2 + 2I_1R_2 = 0$$

$$I_1R_1 = (I - I_1)R_2 = I_2R_2$$

which is KVL for the closed loop ABCD.

[Diagram omitted]

* * * * *

[pp. 3-1 - 3-2]

[3-1]

Chapter 3

Structure of Utility Systems

In the previous chapter, the behavior of electricity in a variety of devices was explored. A number of rules were introduced, chiefly in the form of equations, to make possible the analysis of any circuit. In this chapter, some of the ways in which electric utility networks differ from the simple networks of the previous chapter are explained.

- Electric utilities produce power in generators that rotate electric magnets within a frame housing three equally spaced conducting coils, resulting in three distinct "phases" of electricity that differ in timing from each other by 120°. This "3-phase generation" results in considerable capital and operating economies in transmitting power by reducing the number of conductors and the power losses in each. The algebra for determining the combined effects of the three phases depends on whether they are connected in an arrangement that resembles either the letter Y or a triangle, called a "wye" or "delta" arrangement respectively.

- Numerous transformers are used throughout a utility system to increase voltages for efficient transmission and to decrease them to safe and practical levels for distribution subsystems and end-use devices. For transmission planning and control purposes a local

distribution subsystem can be modeled as a single lumped impedance in parallel with the transmission system.

- Transmission lines have their own impedances that must be taken into account by system planners. In particular, the conductors of a transmission line are inherently inductive especially when heavily loaded, which causes them to absorb reactive power. Reactive power must be supplied to the network in order to offset the inductance of the lines and of certain end-use loads such as industrial motors. This can be produced by generators and transmitted but it is of'ten more economically provided at the site of the reactive load.

  Such reactive power "compensation" is desirable because it reduces the amount of current required to deliver a given mount of real power, and it improves voltage control. It is provided by reactive elements added in parallel (shunt) or series to the transmission lines. A shunt capacitor supplies reactive power while a series inductor **[3-2]** consumes it. Compensation can be either passive (fixed) or active (variable in response to system conditions).

- When power demand changes or system resources are lost due to unplanned disturbances, generator output levels must be adjusted almost instantaneously to keep from over- or under-loading circuits. Conservation of energy dictates that an increase in the electric energy delivered to the loads will cause the kinetic energy (frequency) of the generator turbines to decrease.

Changes in the system frequency as well as in tie-line flows for contractual power exchanges with other utilities can be monitored and used to trigger adjustments to the steam injection into the turbines as needed to restore equilibrium and economical operations. For small changes in load, such adjustments occur in real time under the control of electronic telemetry and feedback mechanisms called Automatic Generation Control. Large changes in load or system status must be anticipated and handled with human intervention.

- Several terms and measurements are used to describe a utility system's ability to accommodate changes in power demand or supply availability. "Reliability" is measured by the probability of loss of service to consumers due to unplanned disturbances to system resources, especially unplanned outages of generating units. Reliability is improved by having redundant generation and transmission capacity and by interconnection with other, adjacent utilities. "Security" refers to the ability of the system to accommodate redirected power flows resulting from a sudden loss (e.g. due to lightning) of the transmission circuit between pairs of buses. "Stability" concerns whether generators will remain in synchronization with each other as they jointly respond to changes in system status. Operating transmission and generation resources below their theoretical capacity limits generally improves security and stability.

* * * * *

[pp. 3-12 - 3-17]

[3-12]
Transmission and Distribution

Figure 3.1 on the next page is a schematic representation of how generation, transmission and distribution resources are configured in a utility system. At the source of electric power, different kinds of energy (kinetic, chemical, nuclear) are converted into electric energy in a three-phase generator producing power at around 15,000 volts. Transformers then step up this voltage to a few hundred thousand volts at a *bus* to the transmission line. A bus is any location where electrical devices have interconnected inputs and outputs. There are buses at the junctions of transmission lines with generators, transformers, other transmission lines and distribution subsystems.

Three-phase transmission lines carry low current, high voltage power through isolated areas, using three or four cables (depending on whether the neutral line is present or not). Typically, voltages of 69,000 Volts or above are deemed transmission level, while conductors operating at or below 13,000 Volts are usually accounted for as part of the distribution system. Near the distribution areas a step-down transformer (substation) decreases the voltage and adds the neutral line that is used in the provision of the single-phase power to consumers. Different types of loads use a different number of phases to **[3-13]** meet their power and voltage needs. Three-phase motors take advantage of the constant instantaneous three-phase power, while resistive devices like stoves and light bulbs use line or phase voltage, according to the size of their requirements.

[Diagram omitted]

The transmission system is electrically isolated from the structure and performance of the distribution systems by step-down substation transformers. For transmission planning purposes this means that regional distribution-level loads can be aggregated and regarded as the effects of a single impedance. Operationally, this electrical isolation makes each distribution region relatively immune to the effects of disturbances in other regions, e.g. when lightning knocks out a distribution line. Changes in the end-use load requirements are conveyed back to the transmission system by the substation transformer through changes in current. An increase in power demand at the customer loads causes an increase in the distribution level current flint induces a corresponding change in the current level on the transmission side of the transformer. These current variations will cause the generators to deliver more or less power as needed, through feedback mechanisms explained below.

Not shown in Figure 3.1 are the important components for transmission system monitoring and protection, such as circuit breakers, capacitor banks, and the system operating center. In addition, this figure depicts only a single path from one generator to the load(s). Any real utility includes several generators interconnected to loads in more of a web-like geometry, with multiple paths on which the power will flow. By virtue of Kirchoff's Laws, power arriving at any bus will distribute itself in part to each of the other circuit paths going out of that bus, in inverse proportion to their respective impedances. This phenomenon is referred to as *loop flow;* it has the consequence that power cannot be directed to flow along specific circuits, e.g. just those owned by a particular

utility or those that happen to be operating at below their rated capacity. Loop flows can become a financial and operating problem when power spreads out over lines not owned by the parties scheduling a power transfer.

Control of Generators

It is critical that generation facilities be able to respond essentially instantaneously to the shifting patterns of electric load and that the transmission system have enough flow capacity and controllable voltage support (reactive power compensation) to serve a wide **[3-14]** range of demand requirements. Much of this control must be automatic, relying on feedback from the system itself to guide the corrective actions. Two indicators of system status are primarily relied upon for much of this *Automatic Generation Control (AGC):* system frequency and tie-line flows.[8]

Contract terms and regulatory requirements, and practical engineering considerations require a utility to provide electric power within a very narrow range of frequencies. Even modest deviation can cause severe damage to generators and to electric equipment designed specifically for 60 cycles per second. Steam turbines in particular are vulnerable to fatigue and cracking if operated away from 60 Hz by as little as $\pm$ 0.05 Hz for even a few minutes. A fully loaded steam turbine may be able to sustain 58 Hz for no

[8]Voltages are also closely monitored in order to protect system stability, but frequency and tie-line changes are the primary barometers for maintaining the economic operation of the system. See Chapter 5 for a fuller discussion of stability.

more than ten minutes cumulatively over its entire operating life.[9]

When the mechanical torque on the turbines (due to the steam or other prime mover) is exactly equal to the opposing electrical torque (arising from the counter-emf in the loops of the generator), the frequency of rotation will be a constant. However, when the power demand changes so that it no longer equals power supplied, the rate of rotation of the generator(s) will automatically increase or decrease as dictated by conservation of energy. For instance, when the load increases, the electrical torque exceeds the mechanical torque, causing the frequency of rotation (hence of the supplied alternating current) throughout the system to decline. More prime mover energy (water flow, steam, etc.) must be supplied to one or more generators to balance the increased power demand. A mechanism on each load-following generator called the *governor* manages these changes in energy input whenever the frequency change exceeds a narrow "deadband" range. A gas-fired peaking plant will have a narrower deadband and a faster response than a baseload coal plant, so the peaking plant will respond first to any short-term variations in load. By adjusting the responsiveness of these generators (called the *droop),* the desired sharing of responsibility across several generators for load changes can be pre-programmed into the system. As will be explained

---

[9]To protect the system and its customers, load shedding is scheduled to occur in the MAIN NERC region in 10% blocks, whenever frequency drops to 59.3, 59.0, and 58.7Hz. See Stambach and Ewart, EPRI EL-6360-L, 1989 for a discussion of frequency tolerances and for operating procedures to manage transmission system dynamics.

further below, this adjustment actually involves two phases. **[3-15]** First the plants' mechanical power is matched to the electrical power demanded, usually in a matter of two to ten seconds. This will not occur at 60 Hz but, at a slightly lower frequency when meeting increased demand. Second, the governor *setpoints* are gradually adjusted over a few minutes to move the system back to 60 Hz. Within certain limits, these adjustments can be done in a fashion that achieves an economic dispatch order among the participating plants.

One very important concern for transmission planners and system operators is maintaining system *stability* at or very near 60 Hz as multiple generators adjust to accommodate a new demand or supply condition. The governor mechanisms cannot usually cause an immediate, direct restoration of the system frequency. Instead, the momentum built up in the turbines when they initially respond to increased loading causes them to overshoot the 60 Hz target a bit. Provided they do not overshoot by too much, the electric torque will act as a brake on the generators and induce a reverse correction. Ideally, these oscillations quickly dampen out and converge on 60 Hz for all generators on the system. If they do not, and the generators fall out of synchronization with each other, voltage variations throughout the system can become erratic and extreme, creating unintended power flows that trigger rapid protective shutdown of overloaded circuits. Again by conservation of energy, this sends very strong feedback signals to the generators, occasionally creating a very

complex problem that results in widespread *voltage collapse*.[10] Thus it is critical that system frequency be tightly controlled.

Most utilities are interconnected with several of their neighboring utilities. This linkage affords considerable capital and operating economies, largely because of economies of scope and the related benefits of risk diversification. With a larger network, more alternative paths are available for moving power to each demand node. With more generators interconnected, the probability of unplanned plant outages flint comprise a significant portion of total load is greatly reduced, so generation capacity reserve margins **[3-16]** per MW of peak load can be lower for a given target level of *reliability*. (Reliability is often measured by the probability that plant outages will make it infeasible to serve the entire power demand. Utilities usually maintain sufficient generation and transmission capacity reserves that this is a very unlikely possibility). The total load of an interconnected system itself is somewhat more stable than that of an individual utility because of imperfect correlation of demand across the large

---

[10]While protracted metropolitan blackouts due to voltage collapse are fairly rare, collapses lasting a few seconds to a minute have occurred roughly once annually throughout the developed world every year since 1970. Most recently (12/14/94), an outage at a 345 kV substation i Idaho (and possibly other events) triggered a cascading outage that affected ten states and British Columbia, causing the WSCC interconnected system to separate into four islands. The power was restored in most areas within a few minutes, though some were out for a few hours. See NERC, August 1991, for a survey of the causes of and planning procedures for coping with this risk, and Electric Utility Week (12/19/94) for details on the WSCC event.

pool of end-users. This allows better utilization of baseload plants to capture their operating economies of scale. All of these pooling benefits improve system reliability and decrease capital and operating costs. In order to manage how such benefits are shared, the interconnected utilities must control the *tie-lineflows* between themselves at their borders. Tie-line flow measurement and management are the second important means of achieving economic performance goals for the transmission and generation system.

Operationally, interconnected or "pooled" utilities are usually managed as several *control areas,* within each of which there is a sufficient number of generators to follow load and to control system frequency and tie-line exchanges. The fie-lines between control areas are used for contractual power flows under pooled dispatch (economy interchange), wheeling arrangements, bulk power sales from one utility to another, and unplanned flows that occur when one utility suddenly needs the slack generation capacity of another for rectifying an emergency condition. Any change from scheduled tie-line flows becomes the basis for centrally controlled (pool level) corrective action (primarily to the generators) in order to assure that one utility does not inadvertently supply replacement power to another without compensation. The adjustments to restore planned fie-line flows are not necessarily the same as those that would restore the system frequency. Such changes in flows or system frequency are called *area control errors* (ACE). The ACE is measured every few seconds at each control area. It is given by:

ACE_j = average frequency in control area$_j$ • bias$_j$
+ net unscheduled tieline flows into or out of area j

The *bias* term captures how many MWs of local generation are typically required to offset a 0.01 Hz frequency shift. This ACE is measured in MW, and it will roughly equal the mount of generation shortfall in a given control area. Because of the governor controls described above, an imbalance in area j may be first met by a load-following unit outside of area j. This will be reflected in ACE_j as a frequency decline and a net scheduled import, while the area(s) supplying the new demand (or replacing the lost supply) in j will measure **[3-17]** a frequency decline and a net export. Exports have the opposite sign of imports, so these ACE measurements will be approximately zero outside of area j. This reveals which area needs to make adjustments, without having to evaluate the state of each and every supply or demand bus within each control area. The AGC system adjusts the setpoints of the governors on plants flint are participating in load-following and frequency regulation to restore each ACE to zero. Tiffs also brings frequency back to 60 Hz.[11]

Computers and electronic telemetry equipment are used to make these kinds of system observations and to help the system controller to maintain economic dispatch of the generators for modest changes in load. These computers are

---

[11]In fact, restoring ACE to zero may not cause frequency to equal precisely 60 Hz, in part because of inaccuracies in estimating control area biases. As a result, utilities may find that a system clock gains or loses a small amount of time over the course of a day, indicating that some inadvertent interchange has occurred. This is generally corrected in kind with subsequent MWs rather than monetary payments. See Wood and Wallenberg, 1984, pp. 291-354, for a discussion of AGC and interchange management.

based at control area centers, of which there were 154 in the U.S. as of 1993.

For large changes in load, such as might arise unexpectedly due to a forced outage or a lighting strike that disables a portion of the transmission network, human anticipation and astute, timely operator intervention are required. The primary defense against such contingencies is to maintain buffers of reserve generation and transmission capacities sufficient to absorb the most severe potential disruptions to the system. A system capable of automatically adapting to any single contingent disruption, i.e. of adjusting without further loss of lines or loads to a new supply-demand balance at 60 Hz, is said to be *secure*.

The design of unbundled electric power services and open access protocols must be sensitive to the fact that generation operations mid transmission control are intimately related. The boundary between the two functions is not a precise one. Generators sometimes have to be adjusted to protect the transmission system, and transmission transactions such as wheeling obligations may alter the security of network operations. Analytically, determining how many MW of transmission flow capacity reserves are required for security and how generation and wheeling can be scheduled to achieve a pattern of power flows consistent with the needed transmission reserve margins requires modeling techniques like those described in the next chapter.

Robert C. McDiarmid *
Cynthia S. Bogarad
Peter J. Hopkins
Spiegel & McDiarmid
1350 New York Ave., NW
Washington, D.C. 20005
(202) 829-4000

Counsel for Respondent
Transmission Access Study Group

Charles G. Cole *
David B. Raskin
Alice E. Loughran
Steptoe & Johnson LLP
1330 Connecticut Ave., N.W.
Washington, D.C. 20036
(202) 429-6270

Counsel for Respondent
Edison Electric Institute

* COUNSEL OF RECORD

Nos. 00-568 & 00-809

Apr 19, 2001

IN THE

Supreme Court of the United States

Supreme Court, U.S.
FILED
APR 19 2001
OFFICE OF THE CLERK

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF ENRON POWER MARKETING, INC. AS PETITIONER IN NO. 00-809

JEFFREY D. WATKISS
BRACEWELL & PATTERSON, L.L.P.
2000 K Street, N.W.
Suite 500
Washington, D.C. 20006
(202) 828-5800

JOSEPH R. HARTSOE
SARAH NOVOSEL
ENRON CORPORATION
1775 I Street, N.W.
Washington, D.C. 20006
(202) 828-3360

LOUIS R. COHEN
Counsel of Record
JOSEPH E. KILLORY, JR.
JONATHAN J. FRANKEL
IJAY PALANSKY
MICHAEL PLOTNICK
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000

Counsel for Petitioner Enron Power Marketing, Inc.

5-1 PM

QUESTIONS PRESENTED IN NO. 00-809

Whether the Federal Energy Regulatory Commission (FERC) has jurisdiction under the Federal Power Act (FPA), 16 U.S.C. §§ 792 *et seq.*, to regulate all transmission of electric energy in interstate commerce, including interstate transmission of electric energy that is sold to retail customers at a "bundled" price.

Whether FERC had jurisdiction and the obligation under the FPA to eliminate pervasive "undue discrimination" in the provision of interstate electric energy transmission services by requiring transmission-owning utilities to provide interstate transmission services on the same terms to all users, for all interstate transmissions, including transmissions bundled with retail sales.

Whether the court of appeals erred in ruling that FERC had discretion to interpret the FPA as denying FERC the necessary jurisdiction to remedy the undue discrimination it had found in the provision of interstate transmission.

PARTIES TO THE PROCEEDING

The list of parties before the court of appeals is set forth at No. 00-809 Pet. App. 683a to 688a.

RULE 29.6 STATEMENT

Enron Corp. is the only publicly held company owning 10% or more of petitioner's stock. The following companies are the parent companies of petitioner:

Enron Corp.

Enron North America Corp.

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED i

PARTIES TO THE PROCEEDING ii

RULE 29.6 STATEMENT iii

TABLE OF AUTHORITIES vii

OPINION BELOW 1

JURISDICTION 2

STATUTES AND RULES INVOLVED 2

STATEMENT 3

A. The Electric Industry 3

B. Statutory Background 6

C. The FERC Orders at Issue 11

D. Proceedings in the D.C. Circuit 16

SUMMARY OF ARGUMENT 18

ARGUMENT 20

I. FERC HAS JURISDICTION OVER ALL INTERSTATE TRANSMISSIONS OF ELECTRIC ENERGY, WHETHER THE ENERGY IS SOLD AT WHOLESALE OR RETAIL, BUNDLED OR UNBUNDLED. 20

A. The Federal Power Act Unambiguously Gives FERC Jurisdiction Over All Interstate Transmissions of Electric Power, Whether for Wholesale or Retail Sale, and Whether Bundled or Unbundled. 21

1. FERC Has Jurisdiction Over Transmissions for Both Wholesale and Retail Sales. 21

TABLE OF CONTENTS — Continued

Page

2. FERC's Jurisdiction Over Interstate Transmissions for Retail Sales Is Not Limited to Transmissions That Are Unbundled for Billing Purposes. 24

B. FERC's Abdication of Jurisdiction Over Interstate Transmissions for Bundled Retail Sales Is an Important Error, Because All Transmissions of Electric Energy on the Interstate Grids Are in Interstate Commerce. 27

II. BY REFUSING TO EXTEND OPEN ACCESS TO BUNDLED RETAIL TRANSMISSIONS, FERC VIOLATED ITS OBLIGATION UNDER THE FEDERAL POWER ACT TO CORRECT THE PERVASIVE DISCRIMINATION IT FOUND. 33

A. FERC's Decision Not To Remedy the Discrimination It Found in Sixty Percent of Pertinent Transmissions Violates Sections 205 and 206 of the Federal Power Act. 34

B. FERC's Excuses for Declining To Address Discrimination in Transmissions for Bundled Retail Sales Are Not Valid. 39

1. FERC's Initial Suggestion That Full Open Access Is Not "Necessary" To Eliminate Undue Discrimination Is Unsupported and Does Not Excuse FERC's Failure To Carry Out the FPA's Command. 39

2. The D.C. Circuit Erred in Sustaining FERC's Jurisdictional Defense of Its Failure To Eliminate the Undue Discrimination That It Found. 43

CONCLUSION 45

TABLE OF AUTHORITIES

CASES

Page(s)

AT&T Corp. v. Iowa Utilities Board, 525 U.S. 366 (1999) 5

Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission, 461 U.S. 375 (1983) 32

Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) 8, 22

Ass'n of American Railroads v. Costle, 562 F.2d 1310 (D.C. Cir. 1977) 35, 38

Associated Gas Distributors v. FERC, 824 F.2d 981 (D.C. Cir. 1987) 34

Burlington Truck Lines, Inc. v. United States, 371 U.S. 156 (1962) 40

Chevron U.S.A. Inc. v. Natural Resources Defense Council, 467 U.S. 837 (1984) 17, 21

City of Kansas City, Missouri v. Department of Housing & Urban Development, 923 F.2d 188 (D.C. Cir. 1991) 40

Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) 29

Enron Power Marketing, Inc. v. Northern States Power Co., 528 U.S. 1182 (2000) 25, 42

Escoe v. Zerbst, 295 U.S. 490 (1935) 35

FPC v. Florida Power & Light, 404 U.S. 453 (1972) 29, 30, 31

FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) 8, 17, 22, 24, 32

FPC v. Southern California Edison Co., 376 U.S. 205 (1964) 8

FPC v. Transcontinental Gas Pipe Line Corp., 365 U.S. 1 (1961) 32

Gulf States Utilities Co. v. FPC, 411 U.S. 747 (1973) 35

TABLE OF AUTHORITIES — Continued

Page(s)

Healy v. The Beer Institute, 491 U.S. 324 (1989) 32
Louisiana Public Service Commission v. FERC, 184 F.3d 892 (D.C. Cir. 1999) 35
Maislin Industries, U.S., Inc. v. Primary Steel, Inc., 497 U.S. 116 (1990) 23, 24
McLaurin v. Prater, 30 F.3d 982 (8th Cir. 1994) 35
Mississippi River Transmission Corp. v. FERC, 969 F.2d 1215 (D.C. Cir. 1992) 27, 38
Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Automobile Insurance Co., 463 U.S. 29 (1983) 40
Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953 (1986) 26
Northern States Power Co. v. FERC, 30 F.3d 177 (D.C. Cir. 1994) 31
Northern States Power v. FERC, 176 F.3d 1090 (8th Cir. 1999), *cert. denied sub nom. Enron Power Marketing, Inc. v. Northern States Power Co.*, 528 U.S. 1182 (2000) 11, 25, 42
Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927) 8, 32
Rocky Mountain Helicopters, Inc. v. FAA, 971 F.2d 544 (10th Cir. 1992) 40
Schurz Communications, Inc. v. FCC, 982 F.2d 1043 (7th Cir. 1992) 40
Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir. 2000) ..... *passim*
United States Telecom Ass'n v. FCC, 227 F.3d 450 (D.C. Cir. 2000) 40

TABLE OF AUTHORITIES — Continued

STATUTES

Page(s)

Natural Gas Act, 15 U.S.C. § 717 *et seq.* 8
15 U.S.C. § 717 2
15 U.S.C. § 717b 22
15 U.S.C. § 717c 2
15 U.S.C. § 717d 2
Federal Power Act, 16 U.S.C. §§ 792 *et seq.* i
16 U.S.C. § 824 ..... *passim*
16 U.S.C. § 824d 2, 8, 9, 17, 34
16 U.S.C. § 824e 2, 9, 17, 33, 34
16 U.S.C. § 824j 2, 11
16 U.S.C. § 824k 2, 11
16 U.S.C. § 824*l* 2
16 U.S.C. § 825*l* 2, 40
Energy Policy Act of 1992, codified in pertinent part at 16 U.S.C. §§ 824j-824m 11
Public Utility Regulatory Policies Act of 1978, 16 U.S.C. §§ 2601 *et seq.* 10
16 U.S.C. § 2601 10
16 U.S.C. § 2611 10
28 U.S.C. § 1254(1) 2
28 U.S.C. § 2101(c) 2

RULES

S. Ct. R. 13 2

LEGISLATIVE MATERIALS

H.R. Rep. No. 74-1318 (1935) 25
S. Rep. No. 74-621 (1935) 23, 25, 33

TABLE OF AUTHORITIES — Continued

Page(s)

Federal Power Act Amendments of 1967, Hearings on H.R. 5348, H.R. 5637, H.R. 7799, H.R. 8426, H.R. 8919, H.R. 9174 Before the Subcommittee on Communications and Power of the House Committee on Interstate and Foreign Commerce, 90th Cong. (1967) 7, 9

Memorandum of Oswald Ryan, General Counsel of the Federal Power Commission, and Dozier A. DeVane, Solicitor of the FPC, in *Public Utility Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Committee on Interstate Commerce*, 74th Cong. (1935) 7

Public Utility Holding Cos., Hearings on H.R. 5423 Before the House Committee on Interstate and Foreign Commerce, 74th Cong. (1935) 23, 30

ADMINISTRATIVE CASES & MATERIALS

Energy Information Administration, United States Department of Energy, 2 *Electric Power Annual 1999* (2000) 5

Energy Information Administration, United States Department of Energy, *Electric Sales and Revenue 1999* (2000) 5

Energy Information Administration, United States Department of Energy, *Financial Statistics of Major U.S. Publicly Owned Electric Utilities 1999* (2000) 5

Florida Power & Light Co., 37 F.P.C. 544 (1967) 5, 6, 9, 29, 31

Middle South Energy, Inc., 26 F.E.R.C. ¶ 63,044, at 65,093, 65,113-14 (1984) 35

TABLE OF AUTHORITIES — Continued

Page(s)

Open Access Same-Time Information System (Formerly Real-Time Information Networks) and Standards of Conduct, Order No. 889, [1991-1996 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,035, at 31,585, 61 Fed. Reg. 21,737 (1996) 43

Pacific Gas & Electric Co., 77 F.E.R.C. ¶ 61,204, at 61,793 (1996) 35

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996) .... *passim*

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-A, [Reg. Preambles] III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997) ..... *passim*

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-B, 81 F.E.R.C. ¶ 61,248, 62 Fed. Reg. 64,688 (1997) 2

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,622 (1995) ..... *passim*

TABLE OF AUTHORITIES — Continued

Page(s)

Public Service Co. of New Mexico, 25 F.E.R.C. ¶ 61,469, at 62,029 (1983) 10
Southern Co. Services, Inc., 83 F.E.R.C. ¶ 61,079, at 61,383 (1998) 35

ARTICLES

Davis Wants State Government to Play Large Role in Resolving Utility Crisis, Wall St. J., Jan. 9, 2001, at A3 42

Steven M. Kramer & Bret A. Sumner, *Electric Reliability in North America: Cross-Border Implications*, 14 Nat. Resources & Env't 81 (1999) 4, 9, 42

Narashima Rao & Richard D. Tabors, *Transmission Markets: Stretching the Rules for Profit and Fun*, 13 Elec. J. 20 (2000) 42

In The Supreme Court of the United States

Nos. 00-568 & 00-809

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF ENRON POWER MARKETING, INC. AS PETITIONER IN NO. 00-809

OPINION BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit is reported at 225 F.3d 667 (D.C. Cir. 2000) and reprinted at No. 00-809 Pet. App. 3a to 121a. Federal Energy Regulatory Commission (FERC) Order No. 888 is reported at F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996). FERC's rehearing

decisions, Order No. 888-A and Order No. 888-B, are reported respectively at III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997), and 81 F.E.R.C. ¶ 61,248, 62 Fed. Reg. 64,688 (1997). Relevant portions of FERC Orders Nos. 888 and 888-A and FERC's Notice of Proposed Rulemaking (NOPR), F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,662 (1995), are reprinted at No. 00-809 Pet. App. 125a to 644a.

JURISDICTION

The court of appeals entered its judgment on June 30, 2000, and issued its order denying a timely filed petition for rehearing on August 22, 2000. On November 20, 2000, Enron Power Marketing, Inc. (Enron), filed a timely petition for a writ of certiorari pursuant to 28 U.S.C. § 2101(c) and S. Ct. R. 13. That petition, No. 00-809, was granted by the Court on February 26, 2001. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTES AND RULES INVOLVED

Sections 201, 205, 206, 211, 212, 213, and 313 of the Federal Power Act (FPA), 16 U.S.C. §§ 824, 824d, 824e, 824j, 824k, 824*l* and 825*l*, are reprinted in the Appendix at No. 00-809 Pet. App. 652a to 681a.

Sections 1, 4, and 5 of the Natural Gas Act (NGA), 15 U.S.C. §§ 717, 717c, and 717d, are reprinted in the Appendix at No. 00-809 Pet. App. 645a to 651a.

Relevant portions of FERC Orders Nos. 888 and 888-A are reprinted in the Appendix at No. 00-809 Pet. App. 125a to 551a.

STATEMENT

This case concerns the authority and obligation of the Federal Energy Regulatory Commission (FERC) to remedy what FERC itself called "the single greatest impediment to competition" in the electric industry. NOPR at 33,049, Pet. App. 558a.[1] In the orders under review, FERC found that vertically integrated utilities that own and control major portions of the interstate transmission grids regularly discriminate against competing power suppliers, denying them equal access to the high voltage lines that carry electricity from generation facilities to local distribution facilities. To remedy this undue discrimination, as it is required to do by the Federal Power Act (FPA), FERC ordered all public utilities to publish an "open access transmission tariff" (OATT) and take transmission for their own *wholesale* sales and *un*bundled retail sales under the same terms as other users. But FERC determined that it lacked jurisdiction to apply this requirement to transmissions sold with generation and distribution at retail for a single "bundled" charge. FERC's failure to extend the OATT to such bundled retail transmissions leaves the undue discrimination unremedied in the market segment that accounts for about 60% of all pertinent interstate transmissions. The result is contrary to FERC's express obligations under the FPA and poses a serious threat to coherent regulation of the Nation's interstate transmission grids.

A. The Electric Industry

The electric industry depends on three kinds of facilities: generation facilities that produce electric energy; distribution

---

[1] All citations in this brief to "Pet. App." are to the Petitioner's Appendix filed with Enron's Petition for a Writ of Certiorari in No. 00-809.

facilities that deliver electric energy to end users; and transmission facilities that carry electricity at high voltages from the generation facilities to the distribution facilities.[2] Today, the transmission facilities in every state (except Alaska, Hawaii, and part of Texas) interconnect into two large reticulated grids, the Eastern and Western Interconnections. *See* Steven M. Kramer & Bret A. Sumner, *Electric Reliability in North America: Cross-Border Implications*, 14 Nat. Resources & Env't 81, 82 (1999) (Kramer & Sumner); *see also* Order No. 888 at 31,781, Pet. App. 305a n.541.

The largest segments of the interstate grids in each state are owned by the vertically integrated public utilities that have traditionally provided electricity to their local customers (their "native loads") on a regulated monopoly basis. *See* Order No. 888 at 31,652, Pet. App. 172a. The utilities use these facilities for bulk transmissions of the electric energy that they sell either at wholesale (i.e., to entities that in turn resell) or at retail (i.e., to end users who receive electricity via the utilities' local distribution systems). Other power suppliers that compete against the vertically integrated utilities depend on the same facilities to carry electricity to their customers.

As an accounting and contractual matter, a utility's sales charges may be either "unbundled" or "bundled." That is, the utility may, by its own choice or pursuant to state law, either present separate charges for the electricity, the transmission service, and the delivery service, or it may "bundle" the costs associated with these separate services

---

[2] Although the broad distinction between high voltage transmission facilities and low voltage distribution facilities is of long standing and generally understood, the exact line is a matter of definition. FERC supplied such a definition in Order No. 888 at 31,771, Pet. App. 282a-283a, and it is not at issue in this Court.

into a single line item charge.[3] At present, approximately 37% of pertinent retail sales were previously sold at wholesale, and almost 97% of all retail sales are made on a "bundled" basis.[4] Thus, the bundled retail sales that are the specific concern of No. 00-809 and this brief account for about 60% of the pertinent usage of the interstate grids.

These contractual and accounting arrangements, however, bear no resemblance to the physical behavior of electricity on the high voltage interstate grids. A quantity of electricity is not a discrete object that flows from a particular source to a particular buyer or user over a particular route, and a supplier generating electricity cannot prescribe the route over the grid that "its" electricity will follow.[5] Each

---

[3] *See AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 394 (1999) (defining "unbundled" as "to give separate prices" for various components of the service rendered).

[4] In 1999, approximately 2.44 billion megawatt hours of electricity were sold at retail by FERC jurisdictional generators: 2.4 billion by investor-owned utilities (IOUs) plus 43 million by independent power producers (IPPs). *See* Energy Information Administration, United States Department of Energy (EIA), *Financial Statistics of Major U.S. Publicly Owned Electric Utilities 1999*, at 3 (2000); EIA, 2 *Electric Power Annual 1999*, at 87 (2000). At most, 915 million of these megawatt hours, or 37.5%, had previously been sold at wholesale. *Id.* (showing 545 million megawatt hours were available for resale by IOUs and 370 million megawatt hours were sold "to Utilities" by IPPs). About 76 million megawatt hours (3% of retail sales) were sold on an unbundled basis, with the remaining 97% sold on a bundled basis. *See* EIA, *Electric Sales and Revenue 1999*, at 3, 245, 255 (2000) (noting that total retail sales were generally made on a bundled basis, and showing transmissions of 76 million megawatt hours sold pursuant to "retail wheeling" programs, i.e., on an unbundled basis). In total, therefore, there are no wholesale or unbundled transmissions associated with almost 60% (1.45 billion of 2.44 billion megawatt hours) of all retail sales.

[5] Unlike, for example, a water supply system, no substance—only energy—flows through the grid, and its flow cannot be routed within the grid. *See Florida Power & Light Co.*, 37 F.P.C. 544, 546 (1967).

interconnection operates as a single pool of energy, into which generating facilities (wherever located) deposit electric energy, and from which customers (wherever located) draw it down.[6] Every connected use draws to some degree on every connected source and to some degree affects the state of the entire system. The frequency of electric energy in the grid is maintained at a standard level, generally 60 cycles per second (or a multiple thereof), by legal and physical arrangements affecting the entire grid and all sources and uses. *See Florida Power & Light Co.*, 37 F.P.C. 544, 548, 564-65 (1967). "[A] load change at any point will have an effect on the instantaneous generation and frequency at every point on the interconnected system." *Id.* at 565. A sudden surge of use in Boston, or a downed high voltage transmission line in New York, impacts electric operations in every state in the Eastern Interconnection. *See id.* at 548-50.

B. Statutory Background

In the early years of the Twentieth Century, in part because electricity could be produced in many places but could not be successfully transmitted over long distances without substantial losses, the electricity business was almost entirely local. *See Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681 (D.C. Cir. 2000) (*TAPS*), Pet. App. 9a; Order No. 888 at 31,639, Pet. App. 141a. Vertically integrated utilities, mostly confined to single states, each generated, transmitted, and distributed their own electricity to

[6] In this respect, the electricity network is very different from, for example, the telephone network. When one telephone caller dials another, the switches in the telephone network establish a dedicated circuit between them that remains open for the length of the call, and all communications between the callers travel over this fixed open pathway. By contrast, when a generating utility contracts with an end user to deliver electricity, nothing travels on any path between them: the utility generates an additional amount of electric energy for the grid, and the end user withdraws a corresponding amount of electric energy from the grid.

their own customers, selling it to them on a bundled basis. "The industry consisted of independent, unassociated, local units [but] its piecemeal and planless development resulted in an uneconomic division of territory, wasteful overlapping of facilities, and lack of engineering and economic unity." Memorandum of Oswald Ryan, General Counsel of the Federal Power Commission (FPC), and Dozier A. DeVane, Solicitor of the FPC (Ryan-DeVane Memorandum), in *Public Utility Holding Company Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce*, 74th Cong. 797 (1935) (*Hearings on S. 1725*).[7] In 1935, only a "fraction of the nation's electric systems were interconnected in interstate networks." *Federal Power Act Amendments of 1967, Hearings on H.R. 5348, H.R. 5637, H.R. 7799, H.R. 8426, H.R. 8919, H.R. 9174 Before the Subcomm. On Communications and Power of the House Comm. on Interstate and Foreign Commerce*, 90th Cong. 4 (1967) (*1967 Hearings*) (statement of Lee C. White, Chairman, FPC). Gradually, however, the utilities found that interconnecting with other utilities enabled them to sell their power in other markets and draw on other generators' electricity to meet local demand, which allowed them to increase the reliability and profitability of their services.

Congress adopted the Federal Power Act to regulate this growing network arrangement. As originally enacted, the FPA took three steps pertinent to the present case. First, the FPA gave the Federal Power Commission (FERC's predecessor) jurisdiction over all "transmission of electric energy in interstate commerce" and all "facilities" used for such transmission. 16 U.S.C. § 824(b)(1). It defined "[e]lectric energy in interstate commerce" as energy "transmitted from a State and consumed at any point outside thereof." 16 U.S.C. § 824(c).

[7] The Ryan-DeVane Memorandum summarizes the history of the industry up to 1935.

Second, the FPA gave the FPC jurisdiction over "the sale of electric energy *at wholesale* in interstate commerce." *Id.* § 824(b) (emphasis added). The phrase "at wholesale" was applied to *sales* in order to provide a "bright line" between sales transactions subject to FPC jurisdiction and sales transactions regulated by the states.[8] The qualifier "at wholesale" was not applied to *transmissions* in interstate commerce, all of which were made subject to the Commission's jurisdiction. *See* Order No. 888 at 31,969, Pet. App. 338a ("statute . . . makes no distinction between wholesale transmission and retail transmission"); *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972) (*LP&L*) (interpreting the parallel provision of the NGA, 15 U.S.C. §§ 717 *et seq.*).[9]

Third, the FPA commanded the FPC to remedy "undue discrimination." Specifically, section 205 of the FPA, 16 U.S.C. § 824d, bars any public utility, "with respect to any transmission or sale subject to the jurisdiction of the Commission," from "grant[ing] any undue preference or advantage to any person or subject[ing] any person to any

---

[8] *See FPC v. Southern California Edison Co.*, 376 U.S. 205, 211 (1964). As the Court there explained, with respect to sales, Congress was responding to the Court's decision in *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927), holding that the Commerce Clause barred states from regulating interstate wholesales. The wholesale/retail "bright line" served to distinguish jurisdictional from nonjurisdictional sales without case-by-case adjudication of Commerce Clause issues. There is no comparable distinction with respect to interstate transmissions, all of which are part of interstate commerce and have been subject to federal regulation since 1935. There is therefore no need for a bright line with respect to transmissions.

[9] All of the provisions of Part II of the FPA pertinent to this case are "in all material respects substantially identical" to parallel provisions of the NGA. *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981) (internal quotation omitted). This Court has an "established practice of citing interchangeably decisions interpreting the pertinent sections of the two statutes." *Id.*

undue prejudice or disadvantage," *id.*, and requires each utility to file tariffs setting forth its "practices," *id.* § 824d(c). Section 206(a), 16 U.S.C. § 824e(a), directs FERC, whenever it determines that a practice is "unjust, unreasonable, unduly discriminatory or preferential," to cure the discrimination: FERC "shall determine the just and reasonable . . . practice . . . to be thereafter observed and in force, and shall fix the same by order."

After the adoption of the FPA, two further developments, intertwined with changes in law, set the stage for the present case. First, the process of interconnection accelerated, spurred by ever-greater needs for more reliable electricity service and by technological developments that made it possible to transmit electricity at high voltages over long distances without unacceptable losses. *See* Order No. 888 at 31,641, Pet. App. 147a. By 1967, "[i]nterconnections, direct and indirect, among utilities [were] a far more vital part of the industry's operations." *See 1967 Hearings* at 118 (statement of Lee C. White, Chairman, FPC).[10] Commentators in 1967 accurately predicted that interconnections would become "still more vital in the future." *Id.* Today, all high voltage electric transmission lines (other than those in the two non-contiguous states and part of Texas) are connected into one or the other of the interstate grids. *See* Kramer & Sumner, *supra* at 82; Order No. 888 at 31,781, Pet. App. 305a n.541. The volume of transmissions subject to FERC's jurisdiction has thus increased many fold, not because of any change in the statute (or its interpretation) but because real-world changes in the physical structure of the electric industry have brought almost all transmission within the jurisdiction defined in 1935. These changes have "made [p]hysically isolated

---

[10] *See Florida Power & Light*, 37 F.P.C. at 557 (Carver, Commissioner, dissenting) (noting that more than 90% of transmission facilities were by then interconnected).

systems . . . a thing of the past." Order No. 888 at 31,641, Pet. App. 147a.[11]

A second, closely related major development since 1935 has been the rise of competition among sources of electric energy. Spurred by the energy shortages of the 1970s, Congress adopted the Public Utility Regulatory Policies Act of 1978, 16 U.S.C. §§ 2601 *et seq.* (PURPA), amending the FPA to encourage the construction and more efficient use of electric generation facilities. PURPA achieved this by requiring traditional utilities to buy power from industrial cogenerators and certain generators using renewable energy sources. *See* Order No. 888 at 31,642, Pet. App. 148a & n.36. These new suppliers began to compete with traditional utility generators. *See* 16 U.S.C. §§ 2601, 2611; Order No. 888 at 31,642, Pet. App. 147a-148a. This small step launched a transformation of the industry such that "[i]n 1992, for the first time, generating capacity added by independent producers exceeded capacity added by utilities." Order No. 888 at 31,643, Pet. App. 151a (citation omitted). Other competing sources also grew, including many traditional utilities that became marketers of electricity outside their "native" areas. *See id.* at 31,639, 31,641, Pet. App. 141a, 147a. Where the generation, transmission, and delivery of power were all once largely local activities, generation and marketing of power became the subjects of increasingly intense interstate competition. *See id.* at 31,635, 31,645-46, Pet. App. 131a-132a, 156a-157a.

To compete, however, these new sources of electric power needed to be able to deliver power from the generators to either wholesale customers or retail distribution points, which meant purchasing transmission services from their chief competitors, the traditional vertically integrated utilities

---

[11] *See also Pub. Serv. Co. of New Mexico*, 25 F.E.R.C. ¶ 61,469, at 62,029, 62,034 (1983).

that continued to own a large percentage of the interstate grids.[12] Congress responded by enacting the Energy Policy Act of 1992 (EPAct), codified in pertinent part at 16 U.S.C. §§ 824j-824m, which, in addition to expanding the ranks of competitive generators to include non-utility "exempt wholesale generators," gave FERC greater authority to order transmission-owning utilities to provide transmission service to competing power suppliers. *See* 16 U.S.C. §§ 824j, 824k; Order No. 888 at 31,644-45, Pet. App. 154a. Specifically, the EPAct "amended section 211 [and 212] of the FPA to give the Commission broader authority to order wheeling [transmission of power for another supplier] on a case-by-case basis." Order No. 888 at 31,673, Pet. App. 191a. As FERC noted, however, this amendment "left unaltered the authorities and obligations of the Commission under sections 205 and 206 . . . to remedy undue discrimination." *Id.* at 31,673, Pet. App. 192a.

C. The FERC Orders at Issue

Vertically integrated utilities that own transmission facilities have the incentive and (absent regulation) the ability to discriminate in crippling ways against competing power suppliers. For example, utilities can reserve their transmission facilities for their own sales and force competing suppliers to make more expensive alternative transmission arrangements, and the utilities can manipulate the transmission "curtailment" process to bar competitors' power from the system during periods of system overload. *See Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999). These and other forms of discrimination have

---

[12] FERC found, "[T]hese entities [new suppliers of power] needed transmission service in order to compete in electricity markets." Order No. 888 at 31,643, Pet. App. 150a. In order for there to be competitive power markets, "all wholesale buyers . . . must have equal access to the transmission grid." NOPR at 33,049, Pet. App. 558a.

state-versus-state impacts: customers in one state frequently are served by generating facilities in (and transmission lines that pass through) other states, and the ability of transmission monopolists to favor their native load can force customers in other states to rely on more circuitous and costly transmission arrangements or to forgo the transactions altogether. To use a very rough analogy (because, among other things, electric energy does not behave like solid objects moving from point to point over fixed paths) it is as if Wal-Mart, Safeway, and other large retailers each owned large segments of the interstate highway system used to transport goods in bulk to their retail stores, and they were able to charge others more for the use of their segments of the highway system than they implicitly charge themselves, and could force other users off the highway system onto inefficient and more costly back roads (or off the road entirely) whenever traffic became congested.

In Order No. 888 and, after rehearing, Order No. 888-A, FERC found that the traditional utilities that own much of the interstate transmission grid were in fact engaged in widespread and entrenched undue discrimination against competing users. FERC further found that the case-by-case authority to order transmission provided by the EPAct amendments to sections 211 and 212 was insufficient to remedy such discrimination and that it must use its broader powers under sections 205 and 206. Then, however, FERC, virtually without explanation, held itself powerless to address the vast majority of the problem.

Findings of Undue Discrimination. FERC found that the utilities that own portions of the transmission grid have inherent incentives to discriminate against other suppliers and are actually doing so:

> [U]tilities owning or controlling transmission facilities possess substantial market power; . . . as profit maximizing firms, they have and will continue to exercise that market power in order to maintain and increase market share, and will thus deny their wholesale customers access to competitively priced electric generation; and . . . these unduly discriminatory practices will deny consumers the substantial benefits of lower electricity prices.

NOPR at 33,052, Pet. App. 566a. Structural characteristics in the industry "make it inevitable that [the transmission-owning utilities] will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors." Order No. 888 at 31,682, Pet. App. 214a; Order No. 888-A at 30,210, Pet. App. 436a. FERC found that vertically integrated utilities have in fact acted on these incentives to harm competitors and competition, as illustrated in the record by an "array of allegations and circumstances raised by customers in individual cases over the years." Order No. 888-A at 30,210, Pet. App. 435a. Examples in the record include refusals to transmit, dilatory tactics amounting to refusals to transmit, and refusals to offer comparable service. *See* Order No. 888 at 31,919-26, Pet. App. 315a-331a.

FERC's (Incomplete) Remedy. FERC understood that under the FPA "it is [FERC's] duty to eradicate unduly discriminatory practices." *Id.* at 31,682, Pet. App. 214a. In this case, FERC determined that a broad remedy was necessary because there was "more than sufficient reason to believe that transmission monopolists . . . will continue to engage in unduly discriminatory practices, unless we fashion a remedy to eliminate their ability and incentive to do so." *Id.* at 31,683, Pet. App. 216a-217a.

The remedy FERC fashioned was "functional unbundling." FERC required every public utility to adopt an "open access transmission tariff" (OATT) dictating the terms of all transmissions for wholesale sales and *un*bundled retail

sales.[13] *Id.* at 31,654, 31,781, Pet. App. 178a, 306a. The terms covered by the tariff include price and other conditions of usage, such as rules of priority when system conditions require curtailment of transmission. *See id.* at 31,721-44, 31,749-50, Pet. App. 254a-264a, 276a-278a; Order No. 888-A at 30,278-79, Pet. App. 456a-60a. FERC also required each utility to "state separate rates for wholesale generation, transmission, and ancillary services." Order No. 888 at 31,654, Pet. App. 178a. In sum, the OATT established that when a utility is selling at wholesale, or at retail on an unbundled basis, it must take transmission for itself on the same terms it offers to others and must reflect the cost of this transmission separately in its bill to the customer.

FERC determined, however, that it did not have authority to extend its functional unbundling remedy to transmissions for bundled retail sales. As a result, the FERC orders permit a vertically integrated utility to transmit its bundled retail sales at no explicit charge; to reserve and schedule its uses of its transmission facilities for such bundled retail sales in ways that freeze out competing uses; and, when physical conditions require imposition of transmission curtailment, to give preference to its own use of the transmission facilities for its own bundled retail sales.

Under FERC's cramped vision of its authority, the open access remedy excludes the roughly 60% of pertinent transmissions that are bundled with retail sales. *See supra* note 4. FERC had previously recognized that failure to

---

[13] FERC initially stated that its rule would apply where the utility is either purchasing or selling at wholesale. *See* Order No. 888 at 31,654, Pet. App. 178a. But, on rehearing, FERC dropped the reference to wholesale purchases. Accordingly, if a utility buys bulk power and resells it at retail on a bundled basis, the OATT requirements do not apply. *See* Order No. 888-A at 30,216-17, Pet. App. 451a-453a. The utility is thus freed from the OATT when using the transmission system to supply its own retail needs.

require utilities to take transmission for their retail sales under the OATT "raises the possibility that . . . transmission service for retail purposes will be superior" to wholesale. NOPR at 33,081-82, Pet. App. 634a. But in Order No. 888, FERC nevertheless concluded that "[a]lthough the [functional] unbundling of retail transmission and generation . . . would be helpful in achieving comparability, we do not believe it is necessary. In addition, it raises numerous difficult jurisdictional issues . . . ." Pet. App. 235a.

FERC offered no explanation in Order No. 888 of its "belie[f]" that application of the OATT to bundled retail sales was not "necessary." In its order on rehearing, Order No. 888-A, FERC did not reassert that regulating transmission for unbundled retail sales was not "necessary"; it relied instead solely on the jurisdictional point. *See* Pet. App. 453a-456a. As to that point, FERC correctly noted that "[u]nlike our jurisdiction over *sales* of electric energy, which section 201 of the FPA specifically limits to sales at wholesale, the statute does *not* limit our *transmission* jurisdiction over public utilities to wholesale transmission." Order No. 888 at 31,781, Pet. App. 305a (emphasis added). Accordingly, FERC said, "when a retail transaction is broken into two products that are sold separately . . . we believe the . . . unbundled transmission service involves *only* the provision of 'transmission in interstate commerce' which, under the FPA, is exclusively within the jurisdiction of [FERC]." *Id.*, Pet. App. 306a. But, in a direct about-face, FERC then said, "when transmission is sold at retail as part and parcel of the delivered product called electric energy, the transaction is a sale of electric energy at retail" and, thus, FERC implied, beyond the agency's jurisdictional reach. *Id.* FERC did not even attempt to explain why the bundling of the cost of electricity and the cost of transmission as an accounting and invoicing matter should be legally determinative of its jurisdiction over the activity of interstate transmission.

D. Proceedings in the D.C. Circuit

On petitions for review, the D.C. Circuit upheld FERC's orders against challenges both that they exceeded FERC's jurisdiction and that they did not go far enough to carry out FERC's statutory obligations to remedy undue discrimination. *See Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681, 687 (D.C. Cir. 2000), Pet. App. 8a-9a. 20a-21a. The State of New York and other parties contended that FERC has no jurisdiction over interstate transmission for *any* retail sales, even unbundled ones; the D.C. Circuit rejected this contention, holding that the Act confers jurisdiction over unbundled interstate transmission of electric energy whether it is then sold at wholesale or retail. *See* Pet. App. 34a-35a. Other parties challenged FERC's authority to remedy the undue discrimination it had found by requiring utilities to grant open access to their facilities used for interstate transmissions, arguing that the FPA did not confer such jurisdiction on FERC; the D.C. Circuit also rejected this argument, finding that FERC had "authority under FPA §§ 205 and 206 to require open access as a generic remedy to prevent undue discrimination." Pet. App. 20a-21a.[14]

Conversely, Enron and other parties challenged FERC's failure to provide a complete or adequate remedy for the undue discrimination FERC had found. Enron noted that most electric energy carried over local utilities' transmission facilities is carried for bundled retail sales, and Enron argued

[14] The Board of Water, Light and Sinking Fund Commissioners of The City of Dalton, Georgia (Dalton) and others argued that the record before FERC did not support its finding of undue discrimination and, therefore, FERC had not satisfied one of the legal prerequisites for prescribing any remedy under section 206. The D.C. Circuit disagreed, concluding that the record supported FERC's finding of undue discrimination that needed a remedy. *See* Pet. App. 21a-23a. This Court denied Dalton's petition for a writ of certiorari. No. 00-800.

that FERC's failure to subject such transmission to the OATT would allow vertically integrated utilities to continue to discriminate in favor of themselves and their own retail sales. Citing the unambiguous text of section 201(b) and this Court's holding in *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621 (1972) (*LP&L*), Enron argued that FERC has jurisdiction to regulate all interstate transmission of electric energy, regardless of whether that energy is then sold at wholesale or retail, unbundled or bundled. Enron further argued that FERC was required by the statute to remedy all of the undue discrimination it found, including discrimination in transmissions bundled with retail sales. *See* 16 U.S.C. §§ 824d, 824e.

The D.C. Circuit rejected Enron's arguments with respect to bundled retail sales. The court conceded that the FPA could be read to assign FERC jurisdiction over transmission for bundled retail sales: "A regulator could reasonably construe transmissions bundled with generation and delivery services and sold to a consumer for a single charge as . . . transmission services in interstate commerce [within FERC's jurisdiction]." Pet. App. 35a. But the court ruled that FERC's finding that it lacked jurisdiction over bundled interstate transmissions was "a permissible policy choice" entitled to deference under *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 842-43 (1984). The court said:

> FPA § 201 gives FERC jurisdiction over transmissions in interstate commerce and sales at wholesale[;] the statute also clearly contemplates state jurisdiction over local distribution facilities and retail sales. The statute is much less clear about exactly where the lines between those activities are to be drawn. . . . FERC's decision to characterize bundled transmissions as part of retail sales subject to state jurisdiction therefore represents a statutorily

permissible policy choice to which we must . . . defer under *Chevron*.

Pet. App. 35a.

SUMMARY OF ARGUMENT

FERC's decision that it did not have jurisdiction to apply the OATT to transmissions for bundled retail sales was contrary to law. The FPA gives FERC jurisdiction over "transmission of electric energy in interstate commerce." There is no exception from this branch of FERC's jurisdiction for electricity that is sold at retail, or for electricity that is sold on a bundled basis. The FPA also commands FERC, upon finding "undue discrimination," to fully remedy the problem. FERC did find undue discrimination in this case, and it prescribed a rule that addressed a fraction of the problem, but it abdicated its responsibility to remedy the remainder.

I. The FPA is clear that FERC's jurisdiction over interstate transmission is plenary and not limited to transmission for wholesale or unbundled sales. Moreover, this Court has interpreted the nearly identical parallel provision of the Natural Gas Act to confer just such plenary jurisdiction over interstate transportation of natural gas. The legislative history also supports this interpretation.

The D.C. Circuit's suggestion that the scope of FERC's jurisdiction presented a "policy choice" ignores the statute and mistakes the relationship between transmission and sale. The court assumed that FERC was required to choose between treating transmissions for bundled retail sales as "interstate transmissions" *or* as components of a bundled retail sale, but such transmissions are clearly *both*, legally as well as factually. Transmission of energy across state borders does not cease to be interstate transmission merely because it is bundled with a sale of energy as an invoicing matter. In addition, FERC regulation of the terms of

interstate transmission is entirely consistent with state regulation of the terms of retail sale, even though the former is a component of the latter: the state is simply required to recognize the FERC-approved terms of interstate transmission (just as it recognizes other FERC determinations of matters within FERC's jurisdiction) when the state sets retail rates and other retail terms.

It is important to confirm FERC's jurisdiction over all interstate transmission of electricity because such transmission is in interstate commerce, and no state can regulate it constitutionally or successfully. This Court has traditionally followed an "engineering and scientific" approach to determine whether a transmission is interstate. Transmission facilities in every state (except Alaska, Hawaii, and part of Texas) are connected into one of two interstate grids. As a result, even if the contractual buyer and seller of a quantity of electricity are located in the same state, the transmission of electricity needed to consummate the sale uses the entire interstate grid and is in interstate commerce. State-by-state regulation of various sections or various uses of the interstate grids would be unworkable as both a legal and practical matter and would be inconsistent with Congress's objective of promoting competition and providing cheap and reliable power to every region of the Nation.

II. FERC is required to act to remedy the undue discrimination it found, and may not exempt interstate transmissions bundled with retail sales. FERC found pervasive undue discrimination by the utilities that own transmission facilities that comprise portions of the interstate grids: such utilities have strong incentives to prefer their own use of the facilities over uses by competing suppliers or to serve other customers, and they have acted on these incentives. The utilities' have denied their competitors the use of needed transmission facilities, denied competitors the ability to offer power of equal reliability to that provided by

the utilities, and discriminated between customers of different classes and in different states.

FERC's statutory obligation to remedy such undue discrimination is explicit and mandatory. Neither of FERC's excuses for failing to carry out this mandate is correct in law, fact, or policy. FERC's suggestion (later withdrawn) that it was not "necessary" to apply the open-access terms and conditions to transmission for bundled retail sales was wholly unexplained and contrary to the facts FERC found in Order No. 888. The bundled interstate transmissions that FERC left untouched constitute almost 60% of the pertinent transmissions on the interstate grids, and there is no reason why undue discrimination to favor bundled retail sales is any less likely, any less important, or any more easily remedied without the OATT than any other part of the discrimination FERC found. FERC's ultimate excuse that the statute could be read to deny it the needed jurisdiction is an impermissible interpretation of unambiguous statutory language and was an abdication of its statutory responsibilities.

ARGUMENT

I. FERC HAS JURISDICTION OVER ALL INTERSTATE TRANSMISSIONS OF ELECTRIC ENERGY, WHETHER THE ENERGY IS SOLD AT WHOLESALE OR RETAIL, BUNDLED OR UNBUNDLED.

FERC's interpretation of its jurisdiction over interstate electric transmissions under the FPA—finding no jurisdiction when the cost of the transmission is bundled with the cost of power at retail—is contrary to the plain language of the statute and this Court's interpretation of nearly identical language in the parallel provision of the Natural Gas Act. The court of appeals asserted that FERC had made a "permissible policy choice," but the statute neither requires nor permits a choice: FERC's jurisdiction over the terms of

interstate transmissions is both mandatory and perfectly consistent with state regulation of the terms of retail sales. Particularly in view of the important effects of the terms of interstate electric transmission on interstate commerce, the D.C. Circuit's affirmance of FERC's abdication of jurisdiction was a serious error.

A. The Federal Power Act Unambiguously Gives FERC Jurisdiction Over All Interstate Transmissions of Electric Power, Whether for Wholesale or Retail Sale, and Whether Bundled or Unbundled.

Section 201(b) of the FPA, 16 U.S.C. § 824(b), explicitly gives FERC jurisdiction, without any stated limitation or qualification, over all interstate transmissions of electric energy. Both FERC and the D.C. Circuit correctly ruled that this section grants jurisdiction over transmissions for both wholesale and retail sales, rejecting the contrary views of various parties. But then both FERC and the D.C. Circuit read into section 201(b) an exception for transmissions that are bundled at retail, thus excluding the majority of pertinent interstate transmissions from Order No. 888's open access remedy. This was error: both the agency and the court were bound by the plain meaning of the statute. *Chevron*, 467 U.S. at 842-43.[15]

1. FERC Has Jurisdiction Over Transmissions for Both Wholesale and Retail Sales.

Section 201(b) grants FERC jurisdiction over (a) "the transmission of electric energy in interstate commerce," and

---

[15] FERC itself found that the statutory grant of federal jurisdiction over all interstate transmissions of electric energy is unambiguous. *See* Order No. 888 at 31,781, Pet. App. 305a ("[S]ection 201 of the FPA, *on its face* . . . gives the Commission jurisdiction over transmission in interstate commerce . . . without qualification.").

(b) "the sale of electric energy at wholesale. . . ." 16 U.S.C. § 824(b). Section 201(a), 16 U.S.C. § 824(a), contains the same two distinct phrases. The words "at wholesale" do not appear in the phrase describing transmission and do not limit FERC's jurisdiction over transmission.

FERC and the D.C. Circuit correctly concluded that FERC's jurisdiction over interstate transmission extends to transmission for retail as well as wholesale sales. FERC held, "Unlike our jurisdiction over sales of electric energy, which section 201 specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission . . . ." Order No. 888 at 31,781, Pet. App. 305a. The D.C. Circuit accepted this finding. *See* Pet. App. 35a.

This interpretation is also compelled by this Court's interpretation of the nearly identical parallel provision of the Natural Gas Act (NGA), 15 U.S.C. § 717b.[16] Section 1(b) of that statute gives FERC jurisdiction over "[1] the transportation of natural gas in interstate commerce, [and] [2] the sale in interstate commerce of natural gas for resale." In *LP&L*, the Court explained that "[e]ach of these is an independent grant of jurisdiction and, though the Act's application to 'sales' is limited to sales of interstate gas for resale, the Act applies to interstate 'transportation' regardless of whether the gas transported is ultimately sold retail or wholesale." 406 U.S. at 636. In keeping with the Court's "established practice of citing interchangeably decisions interpreting the pertinent sections of the two statutes," *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981), the *LP&L* decision would be controlling even if the

[16] The only differences in the language are that the NGA refers to "transportation of natural gas" rather than "transmission of electric energy," and refers to the "sale in interstate commerce of natural gas for resale" rather than "sale of electric energy at wholesale in interstate commerce."

FPA's statutory language were not itself clear. *See Maislin Indus., U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116, 131 (1990) ("Once [this Court has] determined a statute's clear meaning, [it] adhere[s] to that determination under the doctrine of *stare decisis*, and we judge an agency's later interpretation of the statute against our prior determination of the statute's meaning.").

The legislative history of the FPA confirms this interpretation. For example, the Senate Report on the bill that contained section 201 stated, "Jurisdiction is asserted . . . over *all* interstate transmission lines whether or not there is a sale of the energy carried by those lines . . . ." S. Rep. No. 74-621, at 48 (1935) (emphasis added). Congress rejected attempts to limit federal transmission jurisdiction to transmissions for wholesales. For example, representatives of the National Association of Railroad and Utility Commissioners (NARUC, predecessor of a petitioner in No. 00-568) attempted to persuade Congress to limit federal transmission jurisdiction to the small category of transmissions (then one to two percent of all transmissions of electric energy) for wholesales. *See Public Utility Holding Cos., Hearings on H.R. 5423 Before the House Comm. on Interstate and Foreign Commerce*, 74th Cong. 1612-13 (1935) (*Hearings on H.R. 5423*) (statement of H. Lester Hooker, Chairman of the Legislative Comm. of NARUC). NARUC proposed an amendment to section 201(b) stating, "[T]he provisions of this title shall apply only to the transmission and sale at wholesale of electric energy in interstate commerce . . . ." *See id.* at 1660 (statement of John E. Benton, General Solicitor of NARUC). Congress rejected this limiting language and enacted the broader jurisdictional grant still contained in section 201(b). As one witness summarized,

> Whether it be *wholesale or retail*, as I understand it, the transmission of the current from one State to another is interstate commerce. Now, what the

> consequence of that may be is an entirely different matter, but under this bill it is one of the reasons asserted for jurisdiction and I am merely reciting those reasons as part of my case.

Id. at 666 (statement of Preston Arkwright, President of Georgia Power Company) (emphasis added).

2. FERC's Jurisdiction Over Interstate Transmissions for Retail Sales Is Not Limited to Transmissions That Are Unbundled for Billing Purposes.

Section 201(b) contains no words limiting FERC's jurisdiction over retail transmissions to unbundled transmissions. Indeed, there is nothing in the statutory language suggesting that FERC's transmission jurisdiction is in any way qualified by or related to the terms on which the transmitted electric energy is sold. Moreover, this Court's interpretation of the parallel NGA provision in the *LP&L* case is again squarely on point. The gas sales at issue in *LP&L* were "direct" retail sales by the pipeline-owning utility, the equivalent of "bundled" retail sales by a transmission-owning electric utility. This Court rejected the contention that there was any exception from the FPC's transmission jurisdiction for direct sales. *See* 406 U.S. at 636-38. Neither FERC nor the Court may ignore the words of the statute or this Court's prior interpretation of them. *See Maislin Indus., U.S., Inc.*, 497 U.S. at 131.[17]

[17] The specific issue in *LP&L* was whether the FPC had jurisdiction to impose, under conditions of temporary shortage of natural gas supply, an orderly plan of curtailment that would include direct retail sales. This Court reversed a court of appeals ruling that the FPC lacked jurisdiction to curtail deliveries to direct sales customers. *See* 406 U.S. at 636. In the present case, one very important feature of the mandated OATT is that when electric system overload conditions require curtailment of transmission, a transmission-owning utility may not discriminate in favor of its own retail customers and against other generating and marketing companies that have purchased "firm" transmission service. *See* Order No. 888 at 31,748-49, Pet. App. 274a-277a. One court of appeals has already held, erroneously, that FERC does not have the power to impose a curtailment plan that covers interstate transmissions for retail sales. *See Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999), *cert. denied*, 528 U.S. 1182 (2000). FERC opposed Enron's petition for a writ of certiorari in that case, No. 99-916, on the ground that the matter should await the D.C. Circuit's decision in the present case, and the petition was denied.

The legislative history confirms that Congress understood that the FPC's jurisdiction over transmissions in interstate commerce would include transmissions for bundled retail sales. The committee report discussions of transmission in interstate commerce, over which FERC would have jurisdiction, contain no hint of any distinction between transmissions for unbundled and bundled sales. *See* S. Rep. No. 74-621, at 17, 19 (1935); H.R Rep. No. 74-1318, at 7, 27 (1935).

In the orders under review, FERC created an exception for transmission for bundled retail sales found nowhere in the language of the FPA. The D.C. Circuit characterized FERC's ruling as a "policy choice" and deferred to FERC. The court said,

> FPA § 201 gives FERC jurisdiction over transmissions in interstate commerce and sales at wholesale[;] the statute also clearly contemplates state jurisdiction over local distribution facilities and retail sales. The statute is much less clear about exactly where the lines between those activities are to be drawn. A regulator could reasonably construe transmissions bundled with generation and delivery services and sold to a consumer for a single charge as *either* transmission services in interstate commerce *or* as an integral component of a retail

> sale. . . . FERC's decision to characterize bundled transmissions as part of retail sales subject to state jurisdiction therefore represents a statutorily permissible policy choice to which we must . . . defer under *Chevron*.

Pet. App. at 35a (emphasis added).

But there are no such "lines," and the "policy choice" posited by the court of appeals is an entirely false one that has no basis in the statute or fact. The transmissions at issue are *both* interstate transmissions of electric energy, as to which FERC has the authority and the duty to eliminate undue discrimination, *and* (if the utility elects to set a single bundled charge) components of state-regulated bundled retail sales. A transmission in interstate commerce does not cease to be an interstate transmission because of the manner in which the electricity is then sold.

There is nothing illogical or inappropriate about FERC's regulation of interstate transmission merely because its cost becomes a component of the price at which electricity is sold in a bundled retail sale regulated by a state. On the contrary, that is exactly the relationship between FERC regulation of wholesale prices and state regulation of retail prices. The price charged in a FERC-regulated wholesale transaction is a cost to the retailer, which must be recognized by the state regulator in fixing retail prices, but this is in no way inconsistent with the state's plenary jurisdiction over the retail sale as such. As this Court explained in *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 966 (1986), FERC establishes the terms, including price, of wholesales; the state then regulates the prices at which the retailer sells. But whether those retail prices are bundled or unbundled, the state regulator must "recognize a FERC-approved [wholesale] price as a reasonable cost for purposes of retail ratemaking." *Id.* at 973. In *Nantahala*, the principle was applied to the FERC-filed allocation of low- and high-cost wholesale power received by the retailer, but exactly the

same principle can—and must—be applied to the terms on which the retailer receives transmission service.

In sum, FERC's decision in this case to "characterize" some interstate transmissions as subject only to state regulation was contrary to the statute and an abdication of its statutory responsibility.[18]

B. FERC's Abdication of Jurisdiction Over Interstate Transmission for Bundled Retail Sales Is an Important Error, Because All Transmissions of Electric Energy on the Interstate Grids Are in Interstate Commerce.

The electric industry is by many measures the largest and most important industry in the United States, affecting every part of the economy and almost every part of private

---

[18] Ironically, the D.C. Circuit had itself earlier explained one important reason why the FERC interpretation, rejected under the NGA in *LP&L* and reasserted under the FPA in the present case, is necessarily wrong. In *Mississippi River Transmission Corp. v. FERC*, 969 F.2d 1215 (D.C. Cir. 1992), the court ruled that FERC had jurisdiction to regulate a natural gas transportation rate "imbedded in" a bundled retail sale. *MRT*, 969 F.2d at 1219 n.4. Holding that FERC's authority over "such transactions is beyond dispute," the court explained that any other rule would invite manipulation by the utility, which would be able to choose its regulator simply by offering bundled or unbundled pricing of the same product and service:

> As far as the statute is concerned, there would have been no doubt of FERC's section 1(b) authority if MRT, instead of charging a bundled price, had charged separately for transporting the gas and for the gas itself. To accept MRT's position would therefore be tantamount to conferring on private parties the power to decide whether FERC could set the rate for interstate transportation. Private parties would have this power because it would be entirely up to them whether to structure a direct sale and interstate-transportation transaction in terms of a bundled price or separate charges.

Id. at 1217-18.

life. As FERC has at least partially recognized, establishing a transmission system capable of effectively meeting the Nation's energy needs depends on opening the interstate transmission grids to robust competition among suppliers of electricity. *See* Order No. 888 at 31,646, 31,652, Pet. App. 158a, 171a-172a; NOPR at 33,049, Pet. App. 558a; *see also TAPS*, 225 F.3d at 681-82, Pet. App. 10a. But if the decision below stands, no regulatory body, federal or state, will have the authority to eliminate undue discrimination in interstate transmissions for bundled retail sales.

The need for federal regulation of interstate transmission results in part from the physical behavior of electricity in the grid. Electricity does not follow the paths implied in contracts between buyers and sellers or in utility rate schedules. On the contrary, the electric energy on a grid can be conceptualized as a pool to which every connected generation facility contributes and from which every connected user draws.[19] Accordingly, because the transmission facilities in every state except Alaska, Hawaii, and part of Texas are interconnected into one of the two grids, every transmission over any part of either grid is in interstate commerce. Moreover, every public rule or private procedure for the use of any portion of the interstate grid to some degree affects every supplier's and every user's costs and ability to sell or receive reliable power. "Undue discrimination" by the owner of a part of the grid must therefore be eliminated by FERC or not at all.

The FPA and this Court's precedent provide FERC with the authority to regulate effectively. The FPA provides that electric energy "shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof . . . ." *See* FPA § 201(c), 16 U.S.C. § 824(c). The Court has interpreted this definition to include

---

[19] *See supra* pp. 5-6.

any transmission of electric energy over a high voltage transmission line connected to an interstate transmission grid. *See FPC v. Florida Power & Light*, 404 U.S. 453 (1972) (*FP&L*). To determine whether a transmission of electric energy is in interstate commerce as defined in section 201(c), the Court has said it will look to "an engineering and scientific, rather than a legalistic or governmental, test." *See id.* at 454 (quoting *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 529 (1945)) (internal quotations omitted). The determination has never turned on an accounting or invoicing procedure (e.g., bundling) or on the contractual relationship between the supplier and customer, but on a scientific understanding of transmission.

In *FP&L*, this Court, addressing the science, focused on the point of interconnection, the "bus" between facilities connected to an interstate grid. The Court accepted FERC's finding that even though the electric utility's own generation facilities were located in the same state as its customer, because of interconnections electric energy necessarily crossed the state line at the bus. *See id.* at 461-63. Because some electricity generated in a state is necessarily consumed in other connected states, and some electricity consumed in a state is necessarily supplied by generation facilities in other connected states, the Court held that transmissions over the interconnected grid are in interstate commerce. *See id.*; *Florida Power & Light*, 37 F.P.C. 544, 550 (1967) ("there is a commingling of energy from different sources at a bus with the result that energy which flows away from such bus is so fully commingled as to consist of energy which has entered the bus both from interstate and intrastate sources"). As Justice Douglas noted in his dissent in *FP&L*, the decision meant that "every privately owned interconnected

[transmission] facility in the United States . . . is within the FPC's jurisdiction." 404 U.S. at 471.[20]

Although the Court spoke in *FP&L* of electrons crossing state lines, the "engineering and scientific" truth is much broader. Every use of electric energy by a connected user is served by all generators connected to the grid, not by a specific generation source. When facilities are interconnected, electric energy does not travel on a closed path from a particular generator to a specific distribution point. On the contrary, electric energy from all generators connected to the grid forms a pool of energy that services all load requirements throughout the grid. If a utility's generation facility is connected to the grid, its output cannot be segregated for use to serve in-state or any other specific load. "All of the electric energy produced by all the generating units [on an interconnected system] is delivered to the common coordinated and integrated modern transmission

---

[20] The legislative history of the FPA contains explanations to Congress of the precise point that Justice Douglas explained (and against which he protested in dissent) in *FP&L*: that interconnection was sufficient to create interstate transmission. For example, a study prepared by Yale Law School Professor Richard Joyce Smith and presented at the 1935 hearings stated:

> In the absence of far-flung technological tie-ups and financial ententes, electric utilities undoubtedly are in fact local enterprises and the regulatory machinery of the individual State, through periodic revisions, may have been adequate to cope with their activities. But once the industry begins to transcend State boundaries either *by physical interconnections* or by subtle business and financial affiliations the theory of State regulation may become obsolete. . . . Decisions as to the power of the Federal Government to regulate interstate light and power business thus far have assumed that the determinant of interstate business is *physical interconnection* with actual transmission across State boundaries.

Hearings on H.R. 5423, at 77, 97 (emphasis added).

system from which all of the customers are supplied." *Florida Power & Light*, 37 F.P.C. at 566. Viewed differently, "[t]here is no way to determine what path electricity actually takes between two points or indeed whether the electricity at the point of delivery was ever at the point of origin." *See Northern States Power Co. v. FERC*, 30 F.3d 177, 179 (D.C. Cir. 1994).

For the grid to operate, its facilities must be electromagnetically synchronized; that is, all generators must be operated so that they rotate at 60 cycles per second (or a multiple thereof). This "synchronism" is maintained by a combination of automatic and human-controlled measures that respond to changes in both demand and supply. Every use physically affects the entire system, drawing on all sources and, to some degree, employing all of the interstate grid to transmit the power being used. "'[I]f a housewife in Atlanta on the Georgia system turns on a light, every generator on Florida's system almost instantaneously is caused to produce some quantity of additional electric energy which serves to maintain the balance in the interconnected system between generation and load.'" *FP&L*, 404 U.S. at 460 (quoting 37 F.P.C. at 567-68). Similarly, a transmission line that is downed (or taken off line by its owner) in Florida affects the flow of power to users in every state in the Eastern Interconnection. *See* 37 F.P.C. at 567-68.

State regulation clearly could not eliminate the undue discrimination FERC found. First, as a physical matter, since uses of the grids cannot be separated into discrete transmissions from generators to distribution points, each grid must be regulated as an interstate whole. Second, since competing generation facilities, competing suppliers, and different users are located in different states, and transmissions between them involve and affect facilities used by all of them, no state could constitutionally regulate the

terms that give rise to undue discrimination. *See LP&L*, 406 U.S. at 632-33.[21] Third, even to the extent the states could constitutionally promulgate regulations, the inevitable effect of their attempt would be varied and conflicting regulatory programs reflecting the competing interests of different states and their suppliers and users. *See id.* at 632-34 (state regulation of interstate transportation for "direct" sales of gas would "produce a seriously inequitable system" created by an "unavoidable conflict between producing States and consuming States" and the States' incentive to regulate in the "State, not the national interest."); *see also Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983) ("[T]ransmission of energy is an activity particularly likely to affect more than one State, and its effect on interstate commerce is often significant enough that uncontrolled regulation by the States can patently interfere with broader national interests.").

FERC cannot disclaim its statutory authority to regulate all interstate transmissions. "[W]hen [the court] is presented with an attempt by the federal authority to control a problem that is not, by its very nature, one which state regulatory commissions can be expected to deal, the conclusion is irresistible that Congress desired regulation by federal authority rather than nonregulation." *LP&L*, 406 U.S. at 641 (quoting *FPC v. Transcon. Gas Pipe Line Corp.*, 365 U.S. 1, 28 (1961)) (internal quotations omitted). The very reason Congress adopted the FPA was to give the FPC jurisdiction over areas beyond the states' constitutional and practical reach. *See Arkansas Elec.*, 461 U.S. at 384 ("nothing in the language, history, or policy of the Federal Power Act

---

[21] *See Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927); *see also Healy v. The Beer Inst.*, 491 U.S. 324, 336 (1989) ("The critical [constitutional] inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State.").

suggests" that Congress intended to leave an aspect of the industry "unregulated. . . . Congress's purpose in 1935 was to fill a regulatory gap, not to perpetuate one"); S. Rep. No. 74-621, at 17 (noting, in discussing the purpose of the legislation, that both the "regulatory gap" created by *Attleboro* as well as "[o]ther features of this interstate utility business are equally immune from State control either legally or practically"). FERC's denial of its statutory authority threatens Congress's objectives of non-discriminatory, free, and open competition among suppliers and a cheap and reliable supply of power to users in every part of the Nation.

II. BY REFUSING TO EXTEND OPEN ACCESS TO BUNDLED RETAIL TRANSMISSIONS, FERC VIOLATED ITS OBLIGATION UNDER THE FEDERAL POWER ACT TO CORRECT THE PERVASIVE DISCRIMINATION IT FOUND.

As FERC acknowledged in the orders under review, "it is our statutory *obligation* under sections 205 and 206 of the Federal Power Act to remedy undue discrimination," and "[t]o do so, we must eliminate the remaining patchwork of closed and open jurisdictional transmission systems and ensure that *all* these systems . . . cannot use monopoly power over transmission to unduly discriminate against others." Order No. 888 at 31,635, Pet. App. 133a (emphasis added). Moreover, FERC itself held that "[t]he *only* way to effectuate competitive markets and remedy discrimination is through readily available, non-discriminatory transmission access." Order No. 888-A at 30,176, Pet. App. 382a (emphasis added). Yet the final rule FERC adopted exempts transmission included in bundled retail sales from any open access requirements at all.

Where Congress commands an agency to adopt a remedy for all discrimination that it finds, as it did in section 206 of the FPA, 16 U.S.C. § 824e(a), the agency is denied discretion; it may not address only a small fraction of the

problem and then fold its tent. FERC's suggestion in Order No. 888 (abandoned by FERC on rehearing) that open access is not "necessary" for bundled retail transmission was both unsupported and wrong. And FERC's refusal of jurisdiction over the 60% of relevant interstate transmission that is billed as a bundled retail charge is based on a misreading of the FPA.

A. FERC's Decision Not To Remedy the Discrimination It Found in Sixty Percent of Pertinent Transmissions Violates Sections 205 and 206 of the Federal Power Act.

As FERC itself recognized in the orders under review, the Federal Power Act "'fairly bristles' with concern for undue discrimination." Order No. 888 at 31,669, Pet. App. 181a-182a (quoting *Associated Gas Distribs. v. FERC*, 824 F.2d 981, 998 (D.C. Cir. 1987)). Section 205(b) of the FPA forbids any public utility subject to FERC's jurisdiction from "mak[ing] or grant[ing] any undue preference or advantage to any person or subject[ing] any person to any undue prejudice or disadvantage." 16 U.S.C. § 824d(b). If FERC finds such discrimination, section 206(a) of the FPA commands FERC to remedy it:

> Whenever the Commission ... shall find that any rate, charge, or classification demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission *shall* determine the just and reasonable rate, charge, classification, ... practice, or contract to be thereafter observed and in force, and *shall* fix the same by order.

Id. § 824e(a) (emphasis added).

Section 206 is mandatory. Congress directed that FERC "shall" determine and fix a remedy, not that it "may" do so. An agency is required to follow such directives. *See, e.g.*, *Escoe v. Zerbst*, 295 U.S. 490, 493 (1935) ("'shall' ... is the language of command").[22] This Court has recognized that sections 205 and 206 of the FPA are "directives," not guidelines. *Gulf States Utils. Co. v. FPC*, 411 U.S. 747, 759 (1973). Under section 206, "the Commission has the duty—not the option" to remedy whatever unjust, unreasonable, and discriminatory practices it finds. *Louisiana Pub. Serv. Comm'n v. FERC*, 184 F.3d 892, 897 (D.C. Cir. 1999). Indeed, FERC itself has always understood section 206 as a command, not a suggestion. Both the orders under review,[23] and other FERC orders,[24] acknowledge repeatedly that FERC

---

[22] *See also McLaurin v. Prater*, 30 F.3d 982, 984 (8th Cir. 1994) ("the word 'shall' ... is a mandatory command .... '[S]hall' does not mean 'may' or 'is permitted to'; 'shall' has been consistently understood to mean that something is required."); *Ass'n of American Railroads v. Costle*, 562 F.2d 1310, 1312 (D.C. Cir. 1977) (where a statute directs that an agency "shall" regulate, it must do so, because "[t]he word 'shall' is the language of command in a statute").

[23] *See, e.g.*, Order No. 888 at 31,635, Pet. App. 133a ("[I]t is our statutory *obligation* under sections 205 and 206 of the Federal Power Act (FPA) to remedy undue discrimination.") (emphasis added); *id.* at 31,669, Pet. App. 182a-183a (describing the FPA's antidiscrimination "mandates" and concluding that "we have ample legal authority—indeed, a responsibility—under section 206 of the FPA to order the filing of non-discriminatory open access transmission tariffs if we find such order necessary as a remedy for undue discrimination"); *id.* at 31,676, Pet. App. 198a-199a ("Sections 205 and 206 of the FPA *mandate* that we ensure that, with respect to any transmission in interstate commerce ... no person is subject to any undue prejudice or disadvantage.") (emphasis added); *id.* at 31,682, Pet. App. 214a ("it is our *duty* to eradicate unduly discriminatory practices") (emphasis added).

[24] *See Southern Co. Servs., Inc.*, 83 F.E.R.C. ¶ 61,079, at 61,383, 61,386-87 (1998) (quoting Order No. 888); *Pacific Gas & Elec. Co.*, 77 F.E.R.C. ¶ 61,204, at 61,793, 61,819 (1996) (under section 206 FERC has the "obligation" to remedy undue discrimination); *Middle S. Energy, Inc.*,

has a statutory duty to remedy all undue discrimination it finds.

In the orders under review, FERC expressly found the kind of undue discrimination that Congress directed the agency to remedy. FERC specifically found that vertically integrated utilities regularly discriminate by providing themselves and their affiliates transmission superior to the transmission they provide to competing power suppliers. The orders document outright refusals to transmit and delaying tactics used by transmission owners to block competing suppliers from delivering electric energy to customers, as well as inferior service and inferior terms imposed by utilities on competing suppliers who lack transmission alternatives. *See* Order No. 888 at 31,683, 31,926, Pet. App. 215a-216a, 315a-331a. FERC also clearly found that this discrimination will continue unless FERC acts to stop it:

> We conclude that unduly discriminatory and anticompetitive practices exist today in the electric industry and, more importantly, that such practices will increase as competitive pressures continue to grow in the industry, unless the Commission acts now to prevent such practices. . . . The inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices.

---

26 F.E.R.C. ¶ 63,044, at 65,093, 65,113-14 (1984) (section 206 "mandates that the Commission must revise the terms of [contracts among utilities] to eliminate undue preferences or discrimination").

Id. at 31,682, Pet. App. 213a-214a. FERC reaffirmed these findings on rehearing:

> [T]he vast majority of utilities historically have declined to transport electric energy that would compete with their own sales or have offered access that is inferior to what they use for their own sales. . . . [D]iscrimination in transmission services, when viewed in light of utilities' own uses of their transmission systems compared to what they offer third parties, has denied and will continue to deny customers access to electricity at the lowest reasonable rates. The entities on rehearing have raised nothing to persuade us that it is in the interests of consumers to maintain the self-evident incentives for transmission owners to exercise their monopoly power over transmission to discriminate in favor of their own generation sales—incentives that will only increase in the future as competitive pressures continue to escalate.

Order No. 888-A at 30,210, Pet. App. 436a-437a.[25] In making these findings, FERC did not distinguish between bundled and unbundled transmission or suggest that transmission owners' incentives to discriminate depend in any way on how the cost of transmission is accounted for and invoiced at retail.

Notwithstanding these clear findings of pervasive discrimination and Congress's instruction to remedy all undue discrimination it finds, FERC took aim at only a small

---

[25] FERC also noted that this sort of discrimination against independent power suppliers was a subject of particular congressional concern. *See id.* at 30,176, Pet. App. 382a (finding that discrimination, "if permitted to continue, will smother the fledgling competition in electricity markets and undermine the national policies reflected in the Energy Policy Act of 1992 to encourage the development of competitive markets").

slice of the problem and declared victory. Despite finding that the "only way to effectuate competitive markets and remedy discrimination is through readily available, non-discriminatory transmission access," *id.* at 30,176, Pet. App. 382a, FERC refused to extend open access to transmission bundled at the retail level—leaving about 60% of all relevant transmission beyond the reach of the "only" effective remedy. Moreover, FERC's purported solution even for unbundled sales is illusory: unless a state regulator makes retail unbundling mandatory, a vertically integrated utility may opt in or out of open access simply by changing the way it bills its retail customers. An antidiscrimination rule that permits the discriminators to decide whether the rule applies is no rule at all. *See Mississippi River Transmission Corp. v. FERC*, 969 F.2d 1215, 1219 (D.C. Cir. 1992) (observing that interpreting the NGA not to grant FERC jurisdiction over bundled retail transportation of natural gas would "be tantamount to conferring on private parties the right to decide whether FERC could set the rate for interstate transportation. Private parties would have this power because it would be entirely up to them whether to structure a direct sale and interstate-transportation transaction in terms of a bundled price or separate charges").

Where Congress orders an agency to remedy an identified problem, Congress intends the agency to remedy *all* of the problem. *See, e.g., Ass'n of American Railroads v. Costle*, 562 F.2d 1310 (D.C. Cir. 1977) (where Congress directed EPA to promulgate noise emission standards for railroad "equipment and facilities," EPA's regulation of only some "equipment and facilities" did not satisfy its obligation, and the agency was required to regulate further until its obligation was fulfilled). By refusing to adopt any remedy at all for discrimination in transmissions bundled with retail sales, FERC violated section 206 of the FPA.

B. FERC's Excuses for Declining To Address Discrimination in Transmissions for Bundled Retail Sales Are Not Valid.

FERC's attempts to justify its refusal to apply its remedy to interstate transmission for bundled retail sales are unsupported by the record and remarkably terse. A single paragraph in Order No. 888 states, without any explanation or record support, that "[a]lthough the unbundling of retail transmission and generation . . . would be helpful in achieving comparability, we do not believe it is necessary"; in addition, FERC said such unbundling "raises numerous difficult jurisdictional issues" that it did not further discuss. Order No. 888 at 31,699, Pet. App. 235a. On rehearing, in Order No. 888-A, FERC abandoned its earlier "not . . . necessary" remark, deciding instead that it does not have jurisdiction over the interstate transmission component of bundled retail sales. *See* Pet. App. 454a-456a. Neither excuse justifies FERC's failure to carry out the antidiscrimination command of section 206.

1. FERC's Initial Suggestion That Full Open Access Is Not "Necessary" To Eliminate Undue Discrimination Is Unsupported and Does Not Excuse FERC's Failure To Carry Out the FPA's Command.

In Order No. 888, FERC declined to apply the OATT to transmissions for bundled retail sales, stating without explanation that although full open access would be "helpful" to eliminate undue discrimination, it was "not . . . necessary." Pet. App. 235a. FERC did not assert, or offer any evidence, that the problem of undue discrimination in interstate transmission is any less pervasive or less important with respect to transmissions that are sold at retail at a bundled price, nor did it find that discrimination in this segment could be cured by any means other than open access. FERC's carveout thus violated the basic principles of administrative

law that an agency must explain its actions and must base its factual findings on substantial evidence. *See Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 48, 52 (1983) ("an agency must cogently explain why it has exercised its discretion in a given manner"; there must be a "rational connection between the facts found and the choice made") (internal quotation omitted).[26] In this case, not only is FERC's "not . . . necessary" suggestion unsupported by the substantial evidence required by the FPA, *see* 16 U.S.C. § 825*l*, it wholly contradicts the facts that the agency did find.

The orders under review reflect a record establishing that the vertically integrated utilities' monopoly control over the interstate transmission grid has been "the single greatest impediment" to competition in bulk power marketing, NOPR at 33,049, Pet. App. 558a, and that the discriminatory behavior of these utilities threatens to "smother the fledgling competition in electricity markets and undermine the national policies reflected in the Energy Policy Act of 1992 to encourage the development of competitive markets." Order No. 888-A at 30,176, Pet. App. 387a. FERC documented

---

[26] This Court and others have often rejected such conclusory agency pronouncements. *See, e.g., Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 167-68 (1962) (reversing agency action because of the agency's failure to explain election between two remedies: "There are no findings and no analysis here to justify the choice made, no indication of the basis on which the Commission exercised its expert discretion"); *United States Telecom Ass'n v. FCC*, 227 F.3d 450 (D.C. Cir. 2000) (vacating FCC order that did not explain its use of key statutory terms or the basis for its conclusions); *see also Rocky Mountain Helicopters, Inc. v. FAA*, 971 F.2d 544, 547-48 (10th Cir. 1992) (vacating conclusory agency finding as not supported by substantial evidence); *Schurz Communications, Inc. v. FCC*, 982 F.2d 1043 (7th Cir. 1992) (vacating FCC order where agency failed adequately to explain key findings); *City of Kansas City, Missouri v. Dep't of Hous. & Urban Dev.*, 923 F.2d 188, 194 (D.C. Cir. 1991) (finding arbitrary and capricious agency action based on a factual premise contradicted by the agency's record).

example after example of discriminatory conduct: outright refusals to transmit, delay tactics, and inferior terms of service. *See* Order No. 888 at 31,683, 31,919-26, Pet. App. 215a-216a, 315a-331a. And FERC concluded that nothing short of open access was sufficient to remedy this pervasive undue discrimination. *See* Order No. 888-A at 30,176, Pet. App. 382a.

None of these findings distinguishes between transmissions for bundled sales and unbundled sales, and there is no reason to expect any such distinction. A vertically integrated utility has the same control over the transmission facilities that competitors need, and the same ability to discriminate, regardless of how the utility accounts for and bills for its services at retail. For that reason, FERC described the need for open access broadly, suggesting that "all" transmission facilities must move to open access to avoid "benefit[ing] some customers at the expense of others." Order No. 888 at 31,635, Pet. App. 133a; *see also* NOPR at 33,071, Pet. App. 611a ("Unless all public utilities are required to provide non-discriminatory open access transmission, the ability to achieve full wholesale power competition, and resulting consumer benefits, will be jeopardized."). Indeed, in its Notice of Proposed Rulemaking, FERC recognized that limiting open access to unbundled transmission "raises the possibility that the quality of transmission service for retail purposes will be superior to the quality of transmission service offered for wholesale purposes," Pet. App. 634a, but the agency never returned to this concern at any point in its proceedings.

Exempting transmissions for bundled retail sales allows the vertically integrated utilities pervasive unfair advantages in supplying and purchasing electricity. For example:

(a) A utility can reserve superior transmission capacity for its own bundled retail sales, at times even closing its facilities to other transmissions. *See* Order No. 888 at 31,919-26, Pet. App. 315a-331a. Doing so distorts

competition, forcing competitors of the utility to scramble for less direct, less predictable and more expensive transmission options, assuming that any transmission options are available at all. *See* Narashima Rao & Richard D. Tabors, *Transmission Markets: Stretching the Rules for Profit and Fun*, 13 Elec. J. 20, 27 (2000).

(b) The exemption enables the transmission-owning utility to preclude competition for those customers (e.g., computer server farms or hospitals) that need very high levels of service reliability, because utilities are effectively free to impose curtailment plans allowing them to favor their own bundled retail sales under conditions of system constraint.[27]

(c) In addition to anti-competitive behavior by utilities, some states have threatened, in response to predictions of energy shortage, to close "their" portions of the interstate grid to transmissions other than for the in-state utilities that provide electricity to their citizens, attempting in this way to reserve "their" electricity to themselves. *See, e.g., Davis Wants State Government to Play Larger Role in Resolving Utility Crisis*, The Wall Street Journal, Jan. 9, 2001, at A3.

(d) The discrimination resulting from exempting transmissions for bundled retail sales also extends to access to vitally important information about the scheduling and

---

[27] In *Northern States Power*, FERC took the position that even though it did not believe it had jurisdiction over interstate transmissions for bundled retail sales, it could bar transmission-owning utilities from discriminating in favor of such transmissions and against the transmissions for wholesale or unbundled retail sales over which FERC concedes it has jurisdiction. The Eighth Circuit rejected this contention, 176 F.3d at 1095-96, and FERC did not seek this Court's review. Enron, which had intervened in the case, did petition for a writ of certiorari, but FERC and the utility largely resolved their differences in the particular case, and FERC opposed certiorari, which was denied. 528 U.S. 1182 (2000), No. 99-916.

status of the transmission system. The exemption effectively allows vertically integrated utilities exclusive access to important information about the use and availability of their facilities. *See Open Access Same-Time Information System (Formerly Real-Time Information Networks) and Standards of Conduct*, Order No. 889, [1991-1996 Regs. Preambles] F.E.R.C. Stat. & Regs. ¶ 31,035, at 31,585, 31,585-90, 61 Fed. Reg. 21,737, 21,738-40 (1996). This gives them a competitive advantage in planning for and taking advantage of market conditions.

These examples demonstrate that without applying the OATT to all interstate transmissions, including the 60% of pertinent transmissions that are for bundled retail sales, *see supra* note 4, FERC cannot eliminate the undue discrimination it found. In other words, FERC's "not . . . necessary" finding was unsupported and wrong, and cannot excuse FERC's failure to satisfy its mandate under section 206.

2. *The D.C. Circuit Erred in Sustaining FERC's Jurisdictional Defense of Its Failure To Eliminate the Undue Discrimination That It Found.*

On rehearing, in Order No. 888-A, FERC justified its failure to eliminate undue discrimination involving transmissions for bundled retail sales by asserting that it lacks "jurisdiction" over such transmissions. Pet. App. 453a-456a. On petition for review, the D.C. Circuit sustained FERC's declination solely on the jurisdictional ground. The court ruled that FERC's categorization of interstate transmission for bundled retail sales as part of the retail sale, rather than as interstate transmission, was a "permissible policy choice."

This was error. As Enron showed in Part I, no "choice" was needed or called for. FERC's action simply ignores the plain meaning of the statute. An interstate transmission does

not change character, or cease to be within FERC's jurisdiction under the language of the statute, merely because its cost is bundled as an accounting and invoicing matter with the charge for energy and/or delivery in a retail sale. Moreover, there is no reason why FERC cannot or should not regulate the terms of such interstate transmissions, just as it regulates the terms of wholesale transmissions. In either case, the FERC-regulated terms eventually become a component of a state-regulated retail sale, but this means only that states, in accordance with long-established principles, must take FERC's determinations as to matters within its jurisdiction into account when they regulate retail sales.

The most important point is that *only* FERC can eliminate the undue discrimination FERC found in the provision of interstate transmission services. Individual states cannot do this in their regulation of retail sales. Only FERC can require the owners of interstate transmission facilities to serve others on terms as favorable as the terms on which they serve themselves. Only FERC can regulate the operation of the interstate grid in a way that assures open and fair competition, leading to the provision of electricity with the greatest possible reliability at the lowest possible cost in every region. FERC's erroneous interpretation of the statute prevents it from doing so.

CONCLUSION

The decision of the court of appeals sustaining FERC's abdication of jurisdiction over interstate electric transmission for bundled retail sales should be reversed.

Respectfully submitted,

JEFFREY D. WATKISS
BRACEWELL & PATTERSON, L.L.P.
2000 K Street, N.W.
Suite 500
Washington, D.C. 20006
(202) 828-5800

JOSEPH R. HARTSOE
SARAH NOVOSEL
ENRON CORPORATION
1775 I Street, N.W.
Washington, D.C. 20006
(202) 828-3360

LOUIS R. COHEN
Counsel of Record
JOSEPH E. KILLORY, JR.
JONATHAN J. FRANKEL
IJAY PALANSKY
MICHAEL PLOTNICK
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000

Counsel for Petitioner Enron Power Marketing, Inc.

April 19, 2001

Supreme Court, U.S.
FILED
APR 19 2001
CLERK

No. 00-568

In The

Supreme Court of the United States

People of the State of New York and the Public Service Commission of the State of New York, et al.
Petitioners,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

PETITIONERS' BRIEF ON THE MERITS

LAWRENCE G. MALONE *
GENERAL COUNSEL

JONATHAN D. FEINBERG
DIANE T. DEAN
ASSISTANT COUNSEL

PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK
THREE EMPIRE STATE PLAZA
ALBANY, NEW YORK 12223-1350
(518) 474-2510

* Counsel of Record

BECKER GALLAGHER LEGAL PUBLISHING, INC.
CINCINNATI, OH 800-890-5001

QUESTION PRESENTED

Inasmuch as the states in 1935 regulated all aspects of the delivery of electricity to retail customers (including retail transmissions) and Congress, when it enacted the 1935 Federal Power Act (FPA), stated unequivocally that it was not disturbing state regulation, can the 1935 Federal Power Act be read as endorsing FERC preemption of state regulation of the rates, terms and conditions of retail transmissions?

PARTIES

Petitioners joining in this brief are the Public Service Commissions of New York, Florida and Wyoming, the Public Utilities Commissions of Idaho and North Carolina, the New Jersey Board of Public Utilities, the Vermont Board of Public Utilities, the Virginia State Corporation Commission, the Washington Utilities and Transportation Commission, and the National Association of Regulatory Utility Commissioners (NARUC). Pursuant to Rule 29.6, none of the Petitioners/Intervenors State Utility Commissions, which are governmental agencies, needs to file a corporate disclosure statement.

NARUC is a quasi-governmental non-profit corporation organized under the laws of the District of Columbia. It has no corporate parents or affiliates and has not issued shares of stock or debt securities to the public. Within its membership are the governmental bodies of the 50 states engaged in the economic and safety regulation of carriers and utilities. A full list of parties is provided in the Appendix for State Petitioners (States App.) R.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

PARTIES ii

TABLE OF CONTENTS iii

TABLE OF AUTHORITIES viii

OPINIONS BELOW 1

BASIS FOR JURISDICTION 1

STATUTORY PROVISIONS INVOLVED 1

STATEMENT OF THE CASE 4

A. Traditional State Regulation Of Retail Electric Service 4

B. The 1935 Federal Power Act 6

C. FERC's Decision Under Review 7

D. Unbundling And Current State/Federal Regulation 8

E. The D.C. Circuit's Decision 9

SUMMARY OF ARGUMENT 10

ARGUMENT 13

FERC EXCEEDED ITS AUTHORITY WHEN IT ATTEMPTED TO PREEMPT STATE REGULATION OF RETAIL TRANSMISSIONS 13

POINT I 13

THE CIRCUIT COURT APPLIED AN ERRONEOUS STANDARD OF REVIEW 13

POINT II 17

RATHER THAN EVIDENCE A CLEAR AND MANIFEST CONGRESSIONAL INTENT TO AUTHORIZE FERC REGULATION OF AN ESSENTIAL ELEMENT OF RETAIL TRANSACTIONS, THE LEGISLATIVE HISTORY AND LANGUAGE OF THE FEDERAL POWER ACT SHOW THAT CONGRESS INTENDED TO SAFEGUARD PRE-EXISTING STATE REGULATION OF THE DELIVERY OF ELECTRICITY TO RETAIL CUSTOMERS 17

A. The Legislative History And Historical Context Of The Federal Power Act Demonstrate Congress' Intention To Preserve The States' Jurisdiction Over All Aspects Of Retail Service 18

1. FERC Proposed Part II Of The FPA To Fill The "Attleboro gap" 18

2. The States Proposed Various Amendments To FERC's Proposal To Safeguard Pre-Existing State Regulation . . . 20

3. FERC Supported The States' Goal 21

4. Congress Approved FERC's Proposal, With Amendments Proposed By The States To Preserve Pre-Existing State Regulation Over All Aspects Of Retail Service 22

a. Senate And House Committee Reports 22

b. Congressional Floor Debate 24

c. FERC's View Of Its New Authority 25

B. The FPA Limits FERC's Jurisdiction To Wholesale Sales And Associated Transmissions, With Regulation Of All Retail Service Being Reserved To The States 26

1. FERC's Claim To Regulatory Authority Over A Part Of Retail Deliveries Is Not Supported By Any Provision Of The FPA 27

a. Section 201(a) Safeguards Pre-Existing State Regulation . . . 27

b. FERC's Preemption Theory Ignores The Retail/Wholesale "Bright Line" Established By The FPA 28

2. FERC's Claim That Unbundling and § 201(b) Give It Jurisdiction Over Retail Transmission Service Is Not Supported By The FPA 30

a. Section 201(b) Was Not Intended To Authorize FERC Regulation Of Retail Transmission 30

b. FERC's Preemption Theory Is Not Realistic 34

c. FERC's Preemption Theory Is Irrational 35

3. The FPA's Plain Language Unequivocally Defeats FERC's Premise That Essentially All Retail Deliveries On The Interconnected Grid Are In Interstate Commerce 36

a. Jersey Central's Holding That FERC May Regulate Stock Purchases By Public Utilities Does Not Support FERC's Position 37

b. Florida Power & Light's Holding That FERC Could Review Florida Power & Light's Books Does Not Support FERC's Position 42

c. FERC's Reading Of Florida Power & Light And Jersey Central Renders § 201(c) Nearly Nugatory 45

POINT III 46

FERC PREEMPTION OF RETAIL TRANSMISSION WOULD IMPEDE SOUND ENERGY POLICY 46

CONCLUSION 48

TABLE OF AUTHORITIES

Cases

American Textile Mfrs. Inst. v. Donovan,
452 U.S. 490, 513 (1981) 15

Arkansas Elec. Coop. Corp. v. Arkansas Public
Serv. Comm'n, 461 U.S. 375 (1983) 14

AT&T Corp. v. Iowa Utilities Bd.,
525 U.S. 366 (1999.) 8

BFP v. Resolution Trust Corp.,
511 U.S. 531 (1993) 14

Board of Governors of the Federal Reserve
System v. Dimension Financial Corp.,
474 U.S. 361 (1986) 18

Building and Constr. Trades Council of Metro Dist. v.
Associated Builders and Contractors of Mass./R.I.,
507 U.S. 218 (1993) 15

California v. Federal Energy Regulatory Comm'n,
495 U.S. 490 (1990) 14, 16

Chemehuevi Tribe of Indians v. Federal Power Comm'n,
420 U.S. 395 15

Chevron U.S.A. Inc. v. Natural Resources Defense Council,
467 U.S. 837 (1984) 17

Cipollone v. Liggett Group Inc.,
505 U.S. 504 (1992) 14

City of Yonkers v. United States,
320 U.S. 685 (1944) 14-15

Connecticut Light & Power Co. v. Federal Power Comm'n,
324 U.S. 515 (1945) 12, 14, 32, 33

Conroy v. Aniskoff,
507 U.S. 511 (1993) 15

DeBuono v. NYSA-ILA Medical and Clinical Serv.,
520 U.S. 810 (1997) 14

Duquesne Light Co. v. Barasch,
488 U.S. 299 (1989) 48

Federal Power Comm'n v. Florida Power & Light Co.,
404 U.S. 453 (1972) 9, 13, 27, 37, 42-46

Federal Power Comm'n v. Southern California Edison Co.,
376 U.S. 205 (1964) 12, 28, 29, 30

Food and Drug Administration v. Brown and
Williamson Tobacco Co.,
529 U.S. 120, 120 S. Ct. 1291
(2000) 17, 18, 44

Hillsborough County v. Automated Medical Labs, Inc.,
471 U.S., 707 (1985) (quoting Jones v. Rath
Packing Co., 430 U.S. 519 (1977)) . . . 11, 14, 16

Illinois Natural Gas Co. v. Central Illinois Public
Serv. Co., 314 U.S. 498 (1942) 29

Iowa Utilities Bd. v. Federal Communications Comm'n,
219 F.3d 744 (8th Cir. 2000) 17

Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61 (1943) . . . . . *passim*

Jones v. Rath Packing Co., 430 U.S. 519 (1977) 11, 14

Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355 (1986) 13, 15, 21, 32, 47

Matter of Niagara Mohawk Power Corp. v. Public Serv. Comm'n of the State of N.Y., 69 N.Y.2d 365, 507 N.E.2d 287 (1987) 4

Medtronic Inc. v. Lohr, 518 U.S. 470 (1996) 11

New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co., 514 U.S. 645 (1995) 14

Northwestern Elec. Co. v. Federal Power Comm'n, 321 U.S. 119 (1944) 28

Panhandle Eastern Pipeline Co. v. Public Serv. Comm'n, 332 U.S. 507 (1947) 29

Public Utilities Comm'n of Rhode Island v. Attleboro Steam and Elec. Co., 273 U.S. 83 (1927) . . . . . *passim*

Shreveport Rate Cases, Houston, E&WTR Co. v. United States, 234 U.S. 342 (1914) 20, 21

Solid Waste Agency v. Army Corps of Engineers, 531 U.S. 159, 121 S.Ct. 675 (2001) 16

United States v. Bass, 404 U.S. 336 (1971) 14

Wisconsin Public Intervenor v. Mortier, 501 U.S. 601 (1991) 18

Other

Middle South Energy, Inc., 31 FERC ¶ 61, 305 (1985) 28

Niagara Mohawk Power Corporation, 81 FERC ¶ 61, 180 (1997) 35

Portland General Electric Company, 78 FERC ¶ 61, 219 (1997) 36

Statutes

28 U.S.C. § 1254(1) 1

FPA § 201(a), 16 U.S.C. § 824(a) . . . . . *passim*

FPA § 201(b), 16 U.S.C. § 824(b) . . . . . *passim*

FPA § 201(c), 16 U.S.C. § 824(c) 3, 12, 38, 39

FPA § 201(d), 16 U.S.C. § 824(d) 3-4

FPA § 201(e),
16 U.S.C. § 824(e) 4, 38

FPA § 203,
16 U.S.C. § 824b 37, 38, 39

FPA § 204(a),
16 U.S.C. § 824c(a) 37, 39

FPA § 204(f),
16 U.S.C. § 824c(f) 39

FPA § 205,
16 U.S.C. § 824d 4, 12, 21, 36, 40

FPA § 206,
16 U.S.C. § 824e 4

FPA § 206(b) 12, 24, 31

FPA § 206(d),
16 U.S.C. § 824e(d) 24, 36, 40

FPA § 212(h),
16 U.S.C. § 824j(h) 4, 12, 36

Other Authorities

H. Baldridge, The Effect Upon State Powers of Expanded Federal Control in the Public Utility Field,
1 Missouri L. Rev. 245, 256 (1936). 7

Comments of John E. Benton, Solicitor, National Association of Railroad and Utility Commissioners (NARUC),
1935 Hearings on S. 1725 at 760-61, 767, 768 21

Comments of John E. Benton, Solicitor, National Association of Railroad and Utility Commissioners (NARUC),
1935 Hearings on H.R. 5423 at 1654-1657 19-20

Comments of FERC Solicitor DeVane and Senator Hastings,
1935 Hearings on S. 1725 at 250-251 20

Comments of Rep. Monaghan,
1935 Hearings on H.R. 5423 at 761 20

D. DeVane, Highlights of Legislative History of the Federal Power Act of 1935 and the Natural Gas Act, 14 George Washington L. Rev. 31 (1945-46) 26, 34

D. Fink & H. Beaty, Standard Handbook for Electrical Engineers, 2-4 (1987) 46

Hearings Before the Committee on Interstate Commerce, United States Senate, 74th Cong., 1st Sess., on S. 1725 (1935) (1935 Hearings on S. 1725) at 239, 245-46, 253 . . . . . 6, 20

Hearings Before the Committee on Interstate and Foreign Commerce, House of Rep., 74th Cong., 1st Sess., on H.R. 5423 (1935 Hearings on H.R. 5423) at 495, 556 (Testimony of Solicitor Dozier DeVane) 11, 22, 33

House of Rep. Committee on Interstate and Foreign Commerce, Rep. No. 1318, 74th Cong., 1st Sess. (H. Rep. No. 1318) at 7, 8 (1935) 22, 24

A. Mikva & E. Lane., An Introduction to Statutory Interpretation and the Legislative Process (1997) 18

1947 Hearings Before the Committee on Interstate and Foreign Commerce, House of Rep. 84th Cong., 1st Sess. on H.R. 2972, Testimony of FERC Chairman Smith (Hearings on H.R. 2972) at 336 41

1967 Hearings Before the Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce, 90th Cong., 1st Sess, Testimony of FERC Chairman Lee C. White at 125 44

1935 Hearings on H.R. 5423, Testimony of FPC Commissioner Clyde Seavey (speaking for the whole Commission), 384, 399, 401, 402, 495 . . . . . 11-12, 16, 19, 22

79 Congressional Record 8374 (Statement of Senator Hastings)(daily ed. June 6, 1935) 7

79 Congressional Record 8773-8775 (Statement of Senator Wheeler)(daily ed. June 6, 1935) . . 25, 27

79 Congressional Record 10378 (Statement of Congressman Lea)(daily ed. June 28, 1935) . . . 24

79 Congressional Record 10383 (Statement of Congressman Cole) (daily ed. June 28, 1935) 24

R. Sarikas, Introduction to Electrical Theory and Power Transmission, 70, 82 (1995) 46

Senate Committee on Interstate and Foreign Commerce, Rep. No. 62, 74th Cong., 1st Sess. (S. Rep. 621) at 4822 . . . . . 16, 22-23

OPINIONS BELOW

The Opinion of the United States Court of Appeals for the District of Columbia Circuit (States App. C) is Transmission Access Policy Study Group v. Federal Energy Regulatory Comm'n, 225 F.3d 667 (D.C. Cir. 2000). The court's order on rehearing (States App. A) is not officially reported. FERC Order 888 appears at FERC Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540. FERC's rehearing decisions (Orders 888-A and 888-B) are reported, respectively, at FERC Stats. & Regs. ¶ 31,048 and 81 FERC ¶ 61,248 (1997). Pertinent portions of FERC orders are supplied in States App. D through F.

This Court granted Certiorari on February 26, 2001.

BASIS FOR JURISDICTION

The judgment of the Court of Appeals was entered June 30, 2000. The order denying rehearing was issued August 22, 2000 and the petitioner States sought review within 60 days. The grant of Certiorari was issued February 26, 2001. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

16 U.S.C. § 824(a)-(e)
(FPA § 201(a)-(e)) provides:

Declaration of policy; application of subchapter

(a) Federal regulation of transmission and sale of electric energy

It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III of this chapter and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce

(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy or over facilities used in local

distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

(2) The provisions of sections 824i, 824j, and 824k of this title shall apply to the entities described in such provisions, and such entities shall be subject to the jurisdiction of the Commission for purposes of carrying out such provisions and for purposes of applying the enforcement authorities of this chapter with respect to such provisions. Compliance with any order of the Commission under the provisions of section 824i or 824j of this title, shall not make an electric utility or other entity subject to the jurisdiction of the Commission for any purposes other than the purposes specified in the preceding sentence.

(c) Electric energy in interstate commerce

For the purpose of this subchapter, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale" defined

The term "sale of electric energy at wholesale" when used in this subchapter,

means a sale of electric energy to any person for resale.

(e) "Public utility" defined

The term "public utility" when used in this subchapter and subchapter III of this chapter means any person who owns or operates facilities subject to the jurisdiction of the Commission under this subchapter (other than facilities subject to such jurisdiction solely by reason of section 824i, 824j, or 824k of this title).

Other relevant statutory provisions, 16 U.S.C. § 824d (FPA 205), 16 U.S.C. § 824e (FPA 206) and 16 U.S.C. § 824j(h) (FPA 212(h)), are provided in States App. G.

STATEMENT OF THE CASE

A. Traditional State Regulation Of Retail Electric Service

State regulatory commissions are statutorily obligated to assure that customers pay "just and reasonable" rates for electric service. E.g., Matter of Niagara Mohawk Power Corp. v. Public Serv. Comm'n of the State of N.Y., 69 N.Y.2d 365, 369, 507 N.E.2d 287, 289 (1987). Although there are many acceptable methods for setting utility rates (e.g., cost of service; debt service; comparisons to surrounding utilities), commissions often design them to recover reasonable and prudent costs that a utility incurs over a period of time. This methodology entails examination of: (1) revenues the company has earned, or is expected to earn,

at current rates; (2) operating expenditures and depreciation on capital investment; (3) the rate base, or capitalization, upon which the company is allowed to earn a return; and (4) the rate of return needed to cover the company's cost of raising capital.

In paying their electric bills, therefore, retail customers normally reimburse the utility for its costs of:

1. Generating, or purchasing, the electricity (commodity) that the customer consumes during the billing period.

2. Delivering electricity to the customer over transmission (generally high voltage) and distribution (usually lower voltage) lines.

3. Metering the customer's usage.

4. Billing the customer and resolving customer inquiries or complaints.[1]

Most electricity used in the United States is generated in the state where it is used. See, e.g., New York State Independent System Operator, January 2001 Report, Attachment 4-C; Florida Reliability Coordinating Council,

---

[1] The terms commodity, transmission and distribution (or delivery), metering and billing refer to specific elements of retail service. In an unbundled environment (discussed below), each term can be considered a separate service with the commodity, metering and billing (as opposed to delivery) being potentially competitive services.

"2000 Regional Load and Resource Planning" (July 2000) at 33 (www.frcc.com/default.htm); Idaho State Electricity Profile (1998), U.S. Dept. of Energy, Energy Information Admin., www.eia.doe.gov. Tables 1 & 9.

If electricity is consumed by the buyer, the transaction is deemed retail; when the electricity is resold by the buyer, the initial transaction is wholesale.[2] The majority of electric sales in the United States are made by vertically integrated generation, transmission and distribution utilities directly to their retail customers without passing through a wholesaler. Most such utilities, however, do purchase some power on a wholesale market for resale to their retail ratepayers. State regulators generally allow utilities to recover their prudently incurred wholesale commodity costs in retail rates.

B. The 1935 Federal Power Act

The Federal Power Commission (FPC)[3] was created in 1920 (First Annual Report of the Federal Power Commission (FPC First Annual Report) (1921)). It primarily regulated the licensing of hydroelectric facilities. Id. at 5-6. The FERC did not regulate electric rates, which were overseen by the states. Id. at 57; Hearings Before the Committee on Interstate Commerce, United States Senate, 74th Cong., 1st Sess., on S. 1725 (1935) (1935 Hearings on S. 1725) at 239, 253.

---

[2] "Wholesale sales," "retail transmission service," "distribution facilities" and other relevant terms are defined in the Glossary of Terms contained in States App. Q.

[3] The Federal Power Commission (FPC) was renamed the Federal Energy Regulatory Commission (FERC) in 1977. The FPC/FERC will be referred to as FERC throughout this brief.

State regulation of wholesale energy transactions between buyers and sellers in different states ended in 1927, when the Court in Public Utilities Comm'n of Rhode Island v. Attleboro Steam and Elec. Co., 273 U.S. 83, 89 (1927), held that, irrespective of whether the Federal Government regulated wholesale sales between states, the states were barred from doing so by the Commerce Clause. FERC's 1928 Report to Congress recommended legislation to fill the gap (Eighth Annual Report of the Federal Power Commission (1928) at 13), but no bill was introduced until 1932.[4] At that point, Congress reorganized FERC, but did not empower it to regulate wholesale services of public utilities (46 Stat. 797 (1931)).

FERC thereafter conferred with representatives of state commissions (Baldridge, supra at 256) and in 1935 proposed legislation to fill the jurisdictional gap that resulted from Attleboro. After modifying FERC's proposal to safeguard pre-existing state regulation (see 79 Cong. Rec. 8374 (1935) (statement of Senator Hastings)), Congress enacted the Federal Power Act (FPA) authorizing FERC to regulate wholesale sales and associated transmission in interstate commerce (§ 201(b)). The FPA, as amended, stated that "federal regulation is to extend only to those matters which are not subject to regulation by the States" (emphasis added; § 201(a)).

C. FERC's Decision Under Review

In 1998, FERC decided that the FPA's 1935 amendments empowered it to preempt state regulation

---

[4] H. Baldridge, The Effect Upon State Powers of Expanded Federal Control in the Public Utility Field, 1 Missouri L. Rev. 245, 256 (1936).

(including rate regulation) of all interconnected transmissions of electricity (those outside Hawaii, Texas and Alaska). Asserting that (1) Congress had only safeguarded the states' regulation of the retail commodity (electricity itself) and its delivery over distribution lines; (2) when states unbundled the commodity element from a consumer's retail rate, "transmission" became a separate service subject to unqualified FERC jurisdiction over electricity being transmitted in interstate commerce; and (3) all transmissions on the interconnected grid are in interstate commerce, FERC claimed preemptive jurisdiction over the portion of unbundled retail deliveries that it termed transmissions. Joint Appendix ("J.A.") 347-350, States App. D-42-44 (FERC Order 888 at 31,780-81); J.A. 593-94, States App. E-39-40 (FERC Order 888-A at 30,339-40).

D. Unbundling And Current State/Federal Regulation

Unbundling is a change in bill format. AT&T Corp. v. Iowa Utilities Bd., 525 U.S. 366, 394 (1999). A retail electricity bill is unbundled when it separately identifies one or more retail elements (e.g., the commodity). For example, a customer might pay 12 cents per kilowatt-hour (kWh) in a fully bundled bill. If the bill is partially unbundled, the customer might pay 4 cents/kWh for the electricity itself (the commodity), and 8 cents/kWh for delivery, metering and billing.

If a state commission wants to encourage the offering of competitive alternatives to metering or billing, it might unbundle those components of the 12 cent/kWh bundled rate. Thus, the customer might see a bill that charges 4 cents/kWh for the commodity, 1 cent/kWh for metering, 1 cent/kWh for billing and 6 cents/kWh for delivery (transmission and distribution).

Unbundling alone, therefore, does not necessarily alter the total due on a customer's bill, either on a per kilowatt-hour or a monthly usage basis. It is an accounting mechanism that allows customers the option of obtaining one or more retail service elements from competitive providers, instead of the utility.[5]

Prior to FERC's adoption of the order under review, the states set rates to recover utilities' costs for all elements of retail service (e.g., the commodity, delivery, metering and billing). Today, the states that have separately identified the commodity, but continue to bundle transmission, distribution, metering and billing, must incorporate FERC's transmission rate into the non-commodity (bundled metering, billing and delivery) portion of the retail bill.

E. The D.C. Circuit's Decision

On June 30, 2000, a Panel of the D.C. Circuit upheld FERC's preemption of retail transmission.[6] The Panel read Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1972) and Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61, 73 (1943), as holding that FERC had jurisdiction over all unbundled transmissions of electric energy on interconnected grids (225 F.3d at 693-694 (States App. C-30-32)). In the alternative, it determined that FERC's interpretation of its jurisdictional limitations was entitled to deference (225 F.3d at 694-695; States App. C-33-34).

---

[5] Of the 50 states, 25 are in some stage of unbundling retail electric service. See U. S. Dept. of Energy, Energy Information Admin., www.eia.doe.gov.

[6] The relevant portion of the Panel's decision was written by Judge Sentelle (225 F.3d at 679; States App. C-4).

SUMMARY OF ARGUMENT

In attempting to preempt the states' traditional regulation of transmissions of electricity to end-users, FERC has constructed the following syllogism:

> Premise 1 - Congress did not safeguard state regulation of the transmission portion of retail deliveries.
>
> Premise 2 - If the price of the commodity appears separately on an electric bill, then the "jurisdictional lines change," giving FERC jurisdiction of unbundled retail transmissions in interstate commerce (J.A. 349-350, States App. D-44, FERC Order 888 at 31,781).
>
> Premise 3 - All retail transmissions on the interconnected grid are in interstate commerce (J.A. 348, States App. D-43, FERC Order 888 at 31,781).

Conclusion - Therefore, FERC may preempt state regulation of the rates, terms and conditions of all unbundled transmissions of electricity to retail customers on the interconnected grid (J.A. 349-350, States App. D-44, FERC Order 888 at 31,781).

The threshold question is, what standard of review should be applied to FERC's preemption theory. Should FERC's three premises be accepted if they are not irrational, as the Circuit Court reasoned (225 F.3d at 694; States App. C-33-34), or should they be put to a higher test?

When a federal agency attempts to preempt activities traditionally regulated by the states, the Court "'start[s] with the assumption that the historic police powers of the States were not to be superseded . . . unless that was the clear and manifest purpose of Congress'." Hillsborough County v. Automated Medical Labs, Inc., 471 U.S. 707, 715 (1985) (quoting Jones v. Rath Packing Co., 430 U.S. 519, 525 (1977)); Medtronic Inc. v. Lohr, 518 U.S. 470, 485 (1996). FERC, therefore, must show that the 1935 Congress intended: (1) not to safeguard state regulation of retail deliveries (Premise 1); (2) to permit FERC to preempt the transmission part of retail deliveries if the retail bill format were to allow consumers to purchase electric energy from competing suppliers (Premise 2); and (3) that all unbundled transmissions on the interconnected grid are in interstate commerce (Premise 3). As discussed below, if any FERC premise fails, its conclusion fails.

There is no provision in the FPA, or its legislative history, that supports FERC's premise that Congress failed to safeguard state regulation over all aspects of retail service. Section 201(a) denied FERC jurisdiction over "matters . . . subject to regulation by the States" and this Court has held that § 201(a)'s safeguard applies to transmission service. Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61, 74 (1943). FERC stressed to Congress, in proposing the FPA provisions under review, that the states were regulating all aspects of service to retail customers, including transmission and distribution (Hearings Before the Committee on Interstate and Foreign Commerce, House of Rep., 74th Cong., 1st Sess., on H.R. 5423 (1935 Hearings on H.R. 5423) at 556; 1935 Hearings on H.R. 5423, Testimony of FERC Solicitor Dozier DeVane at 495) and that no provision of the FPA undermined that regulation (1935 Hearings on H.R. 5423, Testimony of FERC Commissioner

Clyde Seavey (speaking for the whole Commission, 401) at 402 ["Everything is left to the State Commissions that they are performing now."]. It has also acknowledged to this Court that it "has no authority" to regulate the rates for energy transmitted across state lines "to ultimate consumers" (FERC December 1944 Brief to Supreme Court in Connecticut Light & Power Co. v. Federal Power Comm'n, p. 28). Finally, this Court has held that the FPA draws a bright retail/wholesale jurisdictional line that leaves retail matters to the states. Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205 (1964) (Point II.B.1.).

FERC's second premise also fails. Inasmuch as Congress, by FERC's own admission, did not envision unbundling (J.A. 593-594, States App. E-40, FERC Order 888-A at 30,339-40), it could not have intended the retail/wholesale bright line to change with unbundling (J.A. 347-348, States App. D-42, FERC Order 888 at 31,780; J.A. 400-01, D-100, FERC Order 888 at 31,971-72; J.A. 593-594, E-40, FERC Order 888-A at 30,339-40). Further, inasmuch as FERC has preempted states that unbundle the commodity, but not distribution, FERC's assumption that unbundling isolates transmission from state regulated services is inaccurate. Finally, even if unbundling of the commodity creates a separate transmission service, FERC's second premise still fails because the FPA does not authorize FERC to regulate retail transmission service (Point II.B.2.).[7]

The third premise of FERC's syllogism (a claim that all transmissions are interstate) runs afoul of, among other

[7] Sections 206(b), 205, 201(b), 201(c) and 212(h), when read together and in concert with their legislative history, soundly rebuff FERC's claim that Congress empowered it to regulate retail transmission service.

things, FPA § 201(c). FERC's reliance on dicta from Jersey Central and Florida Power & Light for its third premise is misplaced. As shown below, neither case even remotely supports FERC preemption of retail transmissions (Point II.B.3.).

Finally, FERC's position is not only ultra vires, but an impediment to sound energy policy (Point III).

ARGUMENT

FERC EXCEEDED ITS AUTHORITY WHEN IT ATTEMPTED TO PREEMPT STATE REGULATION OF RETAIL TRANSMISSIONS

The following discussion addresses: the erroneous standard of review followed by the Circuit Court (Point I); the FPA's legislative history (Point II.A.) and its language (Point II.B.); and ramifications of FERC preemption (Point III).

POINT I

THE CIRCUIT COURT APPLIED AN ERRONEOUS STANDARD OF REVIEW

"The critical question in any pre-emption analysis is always whether Congress intended that federal regulation supersede state law." Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355, 369 (1986). When a federal agency seeks to override a system of dual (state/federal) regulation, courts require evidence of congressional intent to allow preemption of the cooperative plan. Louisiana Public Serv. Comm'n v. Federal

Communications Comm'n, 476 U.S. at 374-75 ["To permit an agency to expand its power in the face of a congressional limitation on its jurisdiction would be to grant to the agency power to override Congress."]; California v. Federal Energy Regulatory Comm'n, 495 U.S. 490, 497 (1990) ["Just as courts may not find state measures pre-empted in the absence of clear evidence that Congress so intended, so must they give full effect to evidence that Congress considered, and sought to preserve, the States' coordinate regulatory role in our federal scheme."]. Likewise, if states were regulating an area before Congress enacted a statute upon which a federal agency relies for preemptive power, then the burden of demonstrating congressional intent to authorize federal agency preemption rests with the federal agency seeking to override the traditional state regulation. Hillsborough County v. Automated Medical Labs, Inc., 471 U.S. 707, 713 (1985) (quoting Jones v. Rath Packing Co., 430 U.S. 519, 525 (1977)); Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n, 461 U.S. 375, 377 (1983) [preemption requires a showing of "clear and manifest" congressional purpose]; DeBuono v. NYSA-ILA Medical and Clinical Serv., 520 U.S. 810 (1997); New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co., 514 U.S. 645, 655 (1995); BFP v. Resolution Trust Corp., 511 U.S. 531, 546 (1993); Cipollone v. Liggett Group Inc., 505 U.S. 504, 518 (1992); United States v. Bass, 404 U.S. 336, 349 (1971) [when a statute is alleged to preempt pre-existing state regulation, the statute must evidence a clear congressional purpose to authorize such preemption].

The "clear and manifest purpose," or anti-inference, standard of review essentially refutes claims that Congress might inadvertently preempt pre-existing, traditional state regulation. See Connecticut Light & Power Co. v. Federal

Power Comm'n, 324 U.S. 515, 532 (1944) quoting City of Yonkers v. United States, 320 U.S. 685, 692 (1944) ["'Where a federal agency is authorized to invoke an overriding federal power except in certain prescribed situations and then to leave the problem to traditional state control, the existence of federal authority to act should appear affirmatively and not rest on inference alone'."]. It, therefore, defeats the ability of federal agencies to jerrybuild new, preemptive power by tying technological changes to out-of-context statutory provisions and inferring either that Congress would have endorsed preemption of the traditional state regulation had it known of today's developments or that although Congress did not consider preemption, it inadvertently permitted preemption by assigning a federal agency a particular power, which -- when coupled with subsequent developments -- became preemptive. Chemehuevi Tribe of Indians v. Federal Power Comm'n, 420 U.S. 395, 422-423 [an assertion of "tremendous growth in size and efficiency of the modern thermal-electric power complex and the concomitant increase during the past half century in the quantity of water used by steam plants and change in the nature of that usage. . . . is properly addressed to Congress, not to the courts"]; Building and Constr. Trades Council of Metro. Dist. v. Associated Builders and Contractors of Mass./R.I., 507 U.S. 218, 224 (1993) ["We are reluctant to infer preemption"]; Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355, 376 (1986) ["only Congress can rewrite this statute"]; see American Textile Mfrs. Inst. v. Donovan, 452 U.S. 490, 513 (1981); Conroy v. Aniskoff, 507 U.S. 511, 515 (1993) [a statute is to be read as a whole, since the meaning of statutory language depends on context].

The standard of review requiring a showing of "clear and manifest" congressional purpose to endorse preemption applies to this case because in 1935, when the FPA was

enacted, the states were unquestionably regulating all aspects of retail service, including the delivery of even out-of-state electricity by utilities to retail customers (1935 Hearings on H.R. 5423 at 399; Senate Report No. 621 at p. 48). Rather than allege that the FPA evidences a "clear and manifest purpose of Congress" to endorse federal preemption of state regulation over retail transmissions, FERC has stated that Congress did not consider the question (J.A. 347, States App. D-42, FERC Order 888 at 31,780; J.A. 400-01, States App. D-100, FERC Order 888 at 31,971-72; J.A. 593-595, States App. E-40-41, FERC Order 888-A at 30,339-40).

The Court of Appeals nonetheless deferred to FERC's position that a provision of the FPA designed to limit federal regulation to matters "not subject to regulation by the states" (§ 201(a)) did not safeguard pre-existing state regulation of retail transmission and that although Congress did not contemplate unbundling (J.A. 594, States App. E-40, FERC Order 888-A at 30,340), FERC's authority under § 201(b) to set transmission rates became preemptive power in "[t]oday's unbundled world," id.; see also 225 F.3d at 694; States App. C-33-34. In affirming FERC, therefore, the Circuit Court disregarded Hillsborough by upholding federal agency preemption of pre-existing, traditional state regulation without evidence of supportive congressional intent. The Circuit Court also ignored the teaching of California v. Federal Energy Regulatory Comm'n, 495 U.S. 490 (1990), when it sanctioned FERC's termination of 80 years of state regulation over all aspects of retail deliveries in the face of Congress' directive that FERC not regulate matters "subject to regulation by the States" (§ 201(a)). See Solid Waste Agency v. Army Corps of Engineers, 531 U.S. 159, ___, 121 S. Ct. 675, 683 (2001) [rejecting deference where, inter alia, an "administrative interpretation alters the federal-state framework by permitting federal encroachment upon a

traditional state power"]. In deferring to FERC's reading of § 201(b) as preempting traditional state rate regulation and case law that FERC previously insisted was not relevant to state regulation (discussed below), the Circuit Court failed to follow Iowa Utilities Bd. v. Federal Communications Comm'n, 219 F.3d 744, 756 (8th Cir. 2000), wherein the court held that an agency is estopped from contradicting prior assurances made to the Court. Finally, the Circuit Court's deferral to FERC's reading of § 201(b), and the case law upon which FERC built its preemption theory, ignored the fact that FERC had taken a different position on the statute and these cases in testimony to Congress. See Food and Drug Administration v. Brown and Williamson Tobacco Co., 529 U.S. 120, ___, 120 S. Ct. 1291, 1312-1314 (2000) [a federal agency's prior assurances to Congress are relevant in subsequent jurisdictional disputes].

If the D.C. Circuit had subjected FERC's preemption of retail transmission to the correct standard of review, FERC's preemption would have been annulled.[8]

POINT II

RATHER THAN EVIDENCE A CLEAR AND MANIFEST CONGRESSIONAL INTENT TO AUTHORIZE FERC REGULATION OF AN ESSENTIAL ELEMENT OF RETAIL TRANSACTIONS, THE LEGISLATIVE HISTORY AND LANGUAGE OF THE FEDERAL POWER

---

[8] As shown below, inasmuch as the bases for FERC's preemption theory are irrational, its decision does not pass muster even under the deferential standard of Chevron U.S.A. Inc. v. Natural Resources Defense Council, 467 U.S. 837 (1984).

ACT SHOW THAT CONGRESS INTENDED TO SAFEGUARD PRE-EXISTING STATE REGULATION OF THE DELIVERY OF ELECTRICITY TO RETAIL CUSTOMERS

Inasmuch as the basis of each of FERC's three premises turns on the intention of the 1935 Congress, Section A below will examine relevant legislative history.[9] Section B below, subsections 1-3, will show that each premise is at odds with the language of the FPA.

A. The Legislative History And Historical Context Of The Federal Power Act Demonstrate Congress' Intention To Preserve The States' Jurisdiction Over All Aspects Of Retail Service

1. FERC Proposed Part II Of The FPA To Fill The "Attleboro gap"

Part II of the Federal Power Act was initially drafted by FERC's Solicitor, Dozier DeVane. Mr. DeVane testified to Congress that, with regard to electric rates and service, "[t]he bill simply fills this [Attleboro] gap and that is all"

---

[9] In determining the will of Congress, the Court examines the language of the relevant statute and, when necessary, analyzes the statute's context and legislative history. Food and Drug Administration v. Brown and Williamson Tobacco Corp., 529 U.S. 120, ___, 120 S. Ct. 1291, 1300 (2000); Wisconsin Public Intervenor v. Mortier, 501 U.S. 601 (1991); Board of Governors of the Federal Reserve System v. Dimension Financial Corp., 474 U.S. 361, 368 (1986). See generally, Mikva and Lane, An Introduction to Statutory Interpretation and the Legislative Process, at 27-41 (1997).

(1935 Hearings on H.R. 5423 at 549; emphasis added).[10] See Testimony of Commissioner Seavey, 1935 Hearings on H.R. 5423 at 384. The states, for the most part, supported FERC's goal of filling the jurisdictional gap created by the Attleboro decision because the absence of regulation over wholesale rates affected retail rates. When a utility in one state sold power to another state utility, regulators in the purchasing utility's state were, due to Attleboro, unable to control the prices paid to the out-of-state company and had no access to the seller's records to determine whether a reasonable price had been charged. Moreover, even if the seller was shown to have charged an unreasonable price, retail rate disallowances of portions of the in-state utility's cost of purchasing the energy could jeopardize the financial health of the local utility. Thus, the states needed reasonable wholesale rates, which required that the jurisdictional gap be filled. See Comments of John E. Benton, Solicitor, National Association of Railroad and Utility Commissioners (NARUC), 1935

---

[10] In Mr. DeVane's words:

> There has been considerable discussion here as to what is the purpose of this legislation and the effect it will have upon States and upon State regulation, and in that connection, I wish to say that in the instruction to its representatives that participated in the preparation of this legislation, the Federal Power Commission directed that what it desired to recommend to Congress was legislation that would complement and not supersede State regulation.
>
> Our specific instructions, from our Commission, was [sic] to preserve to the fullest extent State regulation and to draw a law that would complement that regulation as far as Congress could go. (p. 495)

Hearings on H.R. 5423 at 1654-1657; see also Comments of Rep. Monaghan, 1935 Hearings on H.R. 5423 at 761; 1935 Hearings on S. 1725 at 756-757; Comments of FERC Solicitor DeVane and Senator Hastings, 1935 Hearings on S. 1725 at 250-251. The "Attleboro gap," therefore, was constantly brought to the attention of Congress during its deliberations. See, e.g., H. Rep. No. 1318, 74th Cong., 1st Sess., at 17 (1935); 1935 Hearings on S. 1725 at 245-246.

2. The States Proposed Various Amendments To FERC's Proposal To Safeguard Pre-Existing State Regulation

While FERC had conferred with some state officials in developing its proposal, the states remained concerned that in filling the "Attleboro gap," Congress might inadvertently empower FERC to preempt pre-existing state regulation (1935 Hearings on H.R. 5423, Benton Testimony, at 1624; Baldridge, supra, at 256. The source of their misgivings was the Interstate Commerce Commission's preemption of specific intrastate railroad rates to avoid discrimination against interstate commerce. Shreveport Rate Cases, Houston, E&WTR Co. v. United States, 234 U.S. 342 (1914). NARUC Solicitor Benton, therefore, cautioned:

> State commissions do not wish to repeat that [Shreveport Rate Cases] experience in the utility field. Accordingly, they have sought in the amendments to Title II of this bill to separate the field within which the federal regulatory commission may exercise jurisdiction from that which is reserved to the states, and to make that separation so clear and explicit throughout the bill that there may be no opportunity for judicial construction to

> make the legislative purpose miscarry. 1935 Hearings on S. 1725 at 760-761, supra.

Just as the states had asked the 1934 Congress to safeguard state regulation from a reoccurrence of the Shreveport Rate Cases when enacting the 1934 Communications Act (see Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355, 371 (1986)), the states asked the 1935 Congress to amend FERC's proposal (1935 Hearings on H.R. 5423 at 1637). Specifically, Solicitor Benton asked Congress to declare in § 201(a) that FERC jurisdiction over wholesale matters would not extend to services "subject to regulation by the states" and to insert qualifying language in sections granting FERC jurisdiction over specific subjects, such as rate regulation of transmission (§ 205). See Benton, 1935 Hearings on S. 1725 at 767, 768; 1935 Hearings on H.R. 5423 at 1556.

3. FERC Supported The States' Goal

In response to the states' proposed amendments, FERC submitted a memorandum to the Senate, which stated, "the wholesale rates governed by [Attleboro] are the only rates which under this title are to be fixed by the federal commission." 1935 Hearings on S. 1725 at 800.[11] With regard to retail transmission, Solicitor DeVane emphasized that (1) the states were regulating retail transmission, the cost of which represented the major part of retail customers' monthly bills (1935 Hearings on H.R. 5423 at 553, 556); (2) they were doing a splendid job (id. at 498); and (3) the bill

---

[11] See 1935 Hearings on H.R. 5423 at 2143, wherein FERC Solicitor DeVane stated that "the bill does not propose to confer any rate jurisdiction on the Federal Power Commission other than wholesale rates."

did not disturb this regulation (id. at 495, 502). See 1935 Hearings on H.R. 5423 at 548, wherein Solicitor DeVane stated that the bill gave the FPC no "jurisdiction whatever over facilities used in local distribution or the transmission facilities that are used in connection with such local distribution" (emphasis added).

FERC Commissioner Seavey, testifying in support of FERC's proposal, stressed that no pre-existing state regulation would be disturbed ["everything is left to the state commissions that they are performing now" (1935 Hearings on H.R. 5423, Testimony of Clyde Seavey at 402)]. Thus, there is no evidence (much less a "clear and manifest" showing) that Congress authorized FERC to preempt the states' pre-existing regulation of in-state retail transmission.

4. Congress Approved FERC's Proposal, With Amendments Proposed By The States To Preserve Pre-Existing State Regulation Over All Aspects Of Retail Service

a. Senate And House Committee Reports

After the public hearings, the Senate Committee discarded the original bill and submitted a new bill, S. 2796, which narrowed FERC jurisdiction. In recommending S. 2796, congressional staff noted that neither § 201(b), the FPA provision which FERC now cites for preemptive power, nor any other part of the 1935 amendments, took "authority from state commissions" (e.g., House of Rep. Committee on Interstate and Foreign Commerce, Rep. No. 1318, 74th Cong., 1st Sess. (H. Rep. No. 1318) at 8) and that the Act would not "impair or diminish the powers of any state commission." Senate Committee on Interstate and Foreign

Commerce, Rep. No. 62, 74th Cong., 1st Sess. (S. Rep. 621) at 48. The Senate Report also gave full recognition to Mr. Benton's objectives by noting that:

> The revision has . . . removed every encroachment upon the authority of the states . . . . The limitation on the Federal Power Commission's jurisdiction in this regard has been inserted in each section in an effort to prevent the expansion of federal authority over state matters. S. Rep. No. 621 at 18.

The Reports repeatedly stated that the proposed legislation safeguarded all aspects of pre-existing state regulation. For example, Senate Report No. 621 notes at page 48:

> Subsection (a) . . . declares the policy of Congress to extend that regulation to those matters which cannot be regulated by the States and to assist the States in the exercise of their regulatory powers, but not to impair or diminish the powers of any State commission.
>
> ***
>
> Subsection (b) defines the scope of this part of the act and the jurisdiction of the Commission. Its provisions . . . do not apply to the retail sale of any energy in local distribution. This subsection leaves to the states the authority to fix local rates even where the energy moves in interstate commerce . . . the ratemaking powers of the Commission are confined to those wholesale

> transactions which the Supreme Court held in [Attleboro] to be beyond the reach of the States. Jurisdiction is asserted over all interstate transmission lines[12] . . . (id. at 48; emphasis added).

Similar assurances appear throughout the corresponding House Report. H. Rep. No. 1318, 74th Cong., 1st Sess. (1935).

Thus, § 201(a) was changed to limit FERC's regulation "to those matters which are not subject to regulation by the states." See H. Rep. No. 1318 at 8.

b. Congressional Floor Debates

In debating the revised bill, individual members of Congress emphasized that the bill would leave the responsibility of setting retail transmission rates to the states -- even when the transmission crossed state lines. For example, Congressman Lea stated, "[w]here a public utility generates its power in one state and transmits it to another state for its own distribution . . . the Federal Power Commission does not fix the rate of delivery but does give the state commission the information on which the state commission can fix its rates" (emphasis added). 79 Cong. Rec. 10378 (daily ed. June 28, 1935) (statement of Congressman Lea).

In explaining title II, Senator Wheeler stated Congress' intention that "nothing in this act shall in any wise interfere

---

[12] As evidenced by § 206(b), later § 206(d), FERC's jurisdiction over interstate transmission facilities was to be contrasted with its lack of jurisdiction over the retail services carried by those facilities.

with State regulation. We preserved the State regulation completely in the bill, but in title II we made the positive statement that the policy should be not to interfere with State regulation, but to assist and help State regulation." 79 Cong. Rec. 8775 (daily ed. June 6, 1935) (statement of Senator Wheeler). As the House of Representatives concluded debates, Congressman Cole stressed that state jurisdiction would not be subjected to a reoccurrence of Shreveport:

> I doubt if any State commission or State officials familiar with the bill as it is now before you will say that the jurisdiction of the States has not been safeguarded and protected in a fair and lawful way. In doing so we have tried--and I think successfully--to avoid the injection into the Federal control, which this title confers, the extension thereof into intrastate activities in the way that the Shreveport case might permit. 79 Cong. Rec. 10383 (daily ed. June 28, 1935) (statement of Congressman Cole).

c. FERC's View Of Its New Authority

Upon passage of the Federal Power Act, FERC stated that the FPA left all retail regulation -- including retail transmission -- to the states. In FERC's words:

> . . . The act does not give the Federal Commission any authority over local rates for electric service, this function being reserved exclusively to the States . . . . The act authorizes the Federal Power Commission, upon the request of any State commission to

> investigate the cost of production and transmission of electric energy by means of interstate facilities beyond the jurisdiction of the requesting State and to place such desired information at the disposal of the State commission . . . . Thus the State . . . may hereafter enter upon such local rate cases armed with the facts essential to local rate control (emphasis added).

Fifteenth Annual Report of the Federal Power Commission (1935) at 1-2; see D. DeVane Highlights of Legislative History of the Federal Power Act of 1935 and the Natural Gas Act of 1938, 14 George Washington L. Rev. 31, 36-41 (1945-1946) [wherein Solicitor DeVane noted that all aspects of regulation of consumer rates had been left to the state].

Thus, the legislative history and context of the 1935 Act demonstrate that Congress filled the "Attleboro gap" while preserving state regulation of all elements of retail service.

B. The FPA Limits FERC's Jurisdiction To Wholesale Sales And Associated Transmissions, With Regulation Of All Retail Service Being Reserved To The States

As discussed above, FERC's preemption theory rests on three, interdependent premises. First, FERC concedes that Congress preserved state regulation of retail (or direct) sales of the commodity (electricity) and the part of the commodity's delivery that uses a utility's distribution system, but it claims the regulation of retail transmission was taken by Congress from the states and given to FERC. J.A. 349-50, States App. D-44, FERC Order 888 at 31,781; J.A. 392, States

App. D-92-93, FERC Order 888 at 31,968-69; J.A. 593-94, States App. E-39-40, FERC Order 888-A at 30, 339.

The second premise of FERC's preemption theory is that if the rate charged for the commodity appears separately on a retail customer's bill, the commodity's "transmission" becomes a separate retail service, subject to FERC jurisdiction under § 201(b) if it is in interstate commerce. Finally, FERC argues that Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61 (1943) and Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1972), render all transmissions on the interconnected grid interstate. Each premise is addressed below.

1. FERC's Claim To Regulatory Authority Over A Part Of Retail Deliveries Is Not Supported By Any Provision Of The FPA

a. Section 201(a) Safeguards Pre-Existing State Regulation

Section 201(a) provides that FERC's jurisdiction shall "extend only to those matters which are not subject to regulation by the states" (§ 201(a)). In 1935, the states were regulating all aspects of retail deliveries (1935 Hearings on H.R. 5423, Solicitor DeVane at 556, supra). Indeed, inasmuch as the utilities' recovery of transmission and distribution costs represented most of the average retail customer's bill (id.), state regulation of retail deliveries was as important to local communities in 1935 as was state regulation of the commodity. See 79 Cong. Rec. 8773-8774 (daily ed. June 6, 1935) (statement of Senator Wheeler) ["The utility business . . . is essentially a local business and its rates ought to be subject to local regulation whenever and wherever it is possible for them to be so regulated."]; see also 1935

Hearings on H.R. 5423, Testimony of Commissioner Seavey at 393.

Section 201(a) is absolutely consistent with the testimony of FERC Commissioner Seavey to the 1935 Congress that "everything is left to the state commissions that they are performing now" (1935 Hearings on H.R. 5423, Testimony of Clyde Seavey at 402). As discussed below, the Court has held that § 201(a)'s general prohibition, while not nullifying FERC's authority to review utility accounting or financing, does apply to state rate regulation of "generation, transmission and sale" (emphasis added). Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61, 74 (1943); Northwestern Elec. Co. v. Federal Power Comm'n, 321 U.S. 119 (1944). Section 201(a), therefore, discredits FERC's initial premise and its preemption theory. Because Congress safeguarded state regulation of retail[13] transmissions, FERC cannot preempt such regulation.

b. FERC's Preemption Theory Ignores The Retail/Wholesale "Bright Line" Established By The FPA

From 1935 until its issuance of the opinion under review, FERC did not attempt to regulate retail service. Its respect for state regulation of retail services was articulated in several agency decisions (e.g., Middle South Energy, Inc., 31 FERC ¶ 61,305 at p. 61,643 (1985)), which referenced the holding of this Court in Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205, 214 (1964)

[13] Again, in the words of FERC Solicitor DeVane, "the bill does not propose to confer any rate jurisdiction on the Federal Power Commission other than wholesale rates." 1935 Hearings on H.R. 5423 at 2143.

[Congress adopted a test "which denied state power to regulate a sale 'at wholesale to local distributing companies' and allowed state regulation of a sale at 'local rates to ultimate consumers'"].

In confirming the retail/wholesale bright line established by the 1935 Congress, the Court in Federal Power Comm'n v. Southern California Edison recounted two of its decisions interpreting the Natural Gas Act. Illinois Natural Gas Co. v. Central Illinois Public Serv. Co., 314 U.S. 498, 504-505 (1942) ["In applying [a] mechanical test for determining when interstate commerce ends and intrastate commerce begins, this Court has held that the interstate transportation and the sale of gas at wholesale to local distributing companies is not subject to state control of rates [citations omitted] . . . state regulation of local retail rates to ultimate consumers has been sustained where the gas so distributed was purchased wholesale from one who had piped the gas into the state . . . ."] and Panhandle Eastern Pipeline Co. v. Public Serv. Comm'n, 332 U.S. 507, 517 (1947) ["The line of the statute was thus clear and complete. It cut sharply and clearly between sales for resale and direct sales for consumptive uses."].

When one considers: (a) FERC's insistence in proposing the 1935 amendments that it was not disturbing pre-existing state regulation; (b) FERC recognition after enactment of the FPA that all aspects of retail regulation were left to the states; (c) the absence of any assignment in the FPA of retail matters to FERC; (d) § 201(a)'s plain language and this Court's holding in Jersey Central that § 201(a) applies to transmission; and (e) case law recognizing a retail/wholesale bright line, it becomes clear that FERC's claim to jurisdiction of retail transmission service is baseless.

2. FERC's Claim That Unbundling And Section 201(b) Give It Jurisdiction Over Retail Transmission Service Is Not Supported By The FPA

While conceding that the FPA's legislative history contains no evidence of congressional intent to preempt the states' pre-existing regulation of utility rates charged retail electric customers (J.A. 347, States App. D-42, FERC Order 888 at 31,780), FERC's preemption theory assumes that if Congress had envisioned the unbundling of retail transmission, it would have authorized preemption when the commodity was unbundled from transmission (J.A. 349-50, States App. D-44, FERC Order 888 at 31, 781).

a. Section 201(b) Was Not Intended To Authorize FERC Regulation Of Retail Transmission

FERC's rate jurisdiction is set forth in §§ 205 and 206 of the FPA. As originally proposed, § 205 might have been read to empower FERC to set the rates public utilities charge for all transmissions of electric energy. At the request of NARUC Solicitor Benton, however, Congress inserted language limiting FERC's ratemaking jurisdiction over transmission to the specific transmissions "subject to the jurisdiction of the Commission." Thus, as FERC subsequently conceded, "[i]t is only in Section 201(b) that the [transmission] 'jurisdiction of the Commission' is defined and conferred" (September 1963 Federal Power Commission Brief to Supreme Court on Writ of Certiorari in Federal Power Comm'n v. Southern California Edison, pp. 29-30, n.16).

Section 201(b) was intended to assign FERC jurisdiction over interstate transmissions associated with

wholesale transactions. As FERC stated in a memorandum to the Senate, "the wholesale rates governed by [Attleboro] are the only rates which under this title are to be fixed by the federal commission." 1935 Hearings on S. 1725 at 800. See 1935 Hearings on H.R. 5423 at 2143, wherein FERC Solicitor DeVane stated that "the bill does not propose to confer any rate jurisdiction on the Federal Power Commission other than wholesale rates." Thus, inasmuch as Congress only authorized FERC to set transmission rates for wholesale transactions, § 201(b) cannot be read as authorizing FERC to preempt state regulation of retail deliveries.[14]

In addition to authorizing FERC to regulate interstate transmissions associated with wholesale service, § 201(b) denies FERC jurisdiction of "facilities used in local distribution." FERC takes the position that transmission lines used to deliver electricity from a supplier to an end-user are not "used in local distribution" and that this provision, therefore, does not safeguard the states' jurisdiction over transmissions to retail customers (J.A. 426-430, States App. D-123-125, FERC Order 888 at 31,980-81).

Section 201(b)'s denial of FERC jurisdiction over "facilities used in local distribution" should be read in context with § 206(d),[15] which provides:

---

[14] Solicitor DeVane emphasized that (1) the states were regulating retail transmission, the cost of which represented the major part of retail customers' monthly bills (1935 Hearings on H.R. 5423 at 553, 556); (2) they were doing a splendid job (id. at 498); and (3) the bill did not disturb this regulation (emphasis added; id. at 495, 502).

[15] FPA § 206(b) was redesignated § 206(d) by Pub. L. 100-473, § 2, 102 Stat. 2299 (1988).

> The Commission upon its own motion, or upon the request of any State commission . . . may investigate and determine the cost of . . . transmission of electricity energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

In Connecticut Light & Power v. Federal Power Comm'n, 324 U.S. 515 (1945), FERC, relying on then § 206(b) for the proposition that it could assert jurisdiction over, but not regulate the rates of, companies selling out-of-state electricity to retail customers, conceded that the states regulated all aspects of retail transactions -- even when energy was in interstate commerce. December 1944 Brief for the Federal Power Commission, pp. 28-29. Whether a delivery line was designated transmission or distribution was significant for the purpose of determining if the owner of the facility was a "public utility" and, therefore, subject to FERC's general jurisdiction (e.g., accounting, financial review), but the designation of a line as transmission had no significance for determining whether FERC could regulate the rates that the line's owner could charge retail customers for the use of the line to deliver electricity. The transmission versus distribution distinction had no significance -- by FERC's admission -- because FERC had "no authority to establish a rate" for the utility's sale of energy, even "out-of-state energy" over the line if the sale was to "ultimate consumers." Id. at 28. If the 1935 Act denied FERC jurisdiction to set retail rates, even when transmissions were in interstate commerce, then FERC has no statutory basis from which to jerrybuild preemptive power due to unbundling. See Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355, 374 (1986) ["an

agency literally has no power to act, let alone pre-empt the validly enacted legislation of a sovereign State, unless and until Congress confers power upon it"].

FERC's concession in Connecticut Light & Power was consistent with FERC Solicitor DeVane's testimony to Congress that although Congress was being asked to empower FERC to regulate wholesale sales and associated transmissions in interstate commerce "[t]his bill does not give the Commission any jurisdiction whatever over facilities used in local distribution or the transmission facilities that are used in connection with such local distribution" (1935 Hearings on H.R. 5423 at 548; emphasis added). Mr. DeVane's observation that the regulation of retail delivery services was off-limits to FERC was consistent with § 201(a)'s declaration that the FPA only empowered FERC to do what the states could not do (1935 Hearings on H.R. 5423 at 2156).

The flaws in FERC's second premise are further magnified by a review of recent congressional action. Congress in 1992, in order to facilitate FERC regulation of wholesale sales, empowered FERC to order electric utilities, on a case-by-case basis, to carry other suppliers' electricity. It did not, however, empower FERC to infringe on state jurisdiction over retail transmissions. Rather, it stated that "[n]othing in this subsection shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an ultimate consumer" (§ 212(h)).

Thus, Congress in 1935 prohibited FERC from regulating matters, such as retail transmission, that were being regulated by the states in 1935 (§ 201(a)), and denied FERC jurisdiction over transmissions used to facilitate local service (§ 201(b); 1935 Hearings on H.R. 5423 at 501, 548, supra).

In 1992, it declared that FERC's authority to order a utility to open its transmission facilities for wholesale transactions could not impede state authority to regulate retail transmissions (§ 212(h)).

b. FERC's Preemption Theory Is Not Realistic

FERC's conjecture that Congress intended § 201(b) to empower it to set retail transmission rates is utterly unrealistic given that (1) the 1935 Congress was simply empowering FERC to do what the states could not do and (2) the Federal Power Commission -- with about 290 civilian employees in 1935 (Fifty-second Annual Report of the United States Civil Service Commission (1935) at 3)[16] and no ratemaking expertise (First Annual Report of the FPC (1921) at 51, 57; Fifteenth Annual Report of the FPC (1935) at 1) -- was in no position to regulate retail transmission rates across the nation.[17] Twelve years later, when asked whether the Federal Government was better equipped than the states to regulate retail rates and services, FERC's Assistant General Counsel stated, "I definitely say, no" (1947 Hearings on H.R. 2972 at 575).[18]

---

[16] The New York Public Service Commission alone had 382 employees in 1935. Laws of New York, 158th Sess. Vol. 1-2 (1935) at 242.

[17] FERC had to draw on other agencies, including the Departments of War, Interior and Agriculture, for even routine licensing oversight (Fifteenth Annual Report of the Federal Power Commission (1935) at 9).

[18] See "Highlights of Legislative History of the Federal Power Act of 1935 and the Natural Gas Act of 1938," 14 George Washington L. Rev. 31, 40 (1945-1946) [wherein Mr. DeVane acknowledged not only that FERC regulation under the FPA was limited to wholesale rates, but that regulation of wholesale electric

c. FERC's Preemption Theory Is Irrational

Unbundling, as indicated above, is an itemization of retail electric customers' bills to encourage competition for an "unbundled" service. By FERC's admission, the 1935 Congress did not contemplate "[t]oday's unbundled world" (J.A. 594, States App. E-40, FERC Order 888-A at 30,339-40). Yet, FERC insists that with unbundling, "the jurisdictional lines change" (J.A. 350, States App. D-44, FERC Order 888 at 31,781). The irrationality of FERC's thinking is underscored by how and when unbundling changes the federal/state scheme.

First, as to how, FERC reasons that unbundling of the commodity creates a separate transmission service. Separating the commodity, but leaving transmission with distribution, metering and billing admittedly reduces by one the number of elements being bundled, but it does not isolate transmission service.

Second, as to when, as indicated, FERC's preemption theory is grounded in an assumption that Congress safeguarded state regulation of the retail commodity and retail distribution, but not retail transmission (J.A. 349-350, States App. D-44, FERC Order 888 at 31,781; J.A. 391-92 States App. D-92-93, FERC Order 888 at 31,969; J.A. 593-94, States App. E-39-40, FERC Order 888-A at 30,339). Such an assumption (that FERC may regulate retail transmissions) brings into question why bundling the commodity with retail transmissions would prevent FERC from preempting transmission, but bundling retail distribution with transmission would not do the same. See Niagara Mohawk Power

---

rates was expected to be a minor FERC undertaking].

Corporation, 81 FERC ¶ 61,180 at p. 61,776 (1997) [wherein FERC stated that a utility need not separately show distribution and transmission on the bill]; see also Portland General Electric Company, 78 FERC ¶ 61,219 at p. 61,950-51 & nn.2-3, n.6 (1997). Inasmuch as electricity is useless unless it is delivered, why is the commodity or distribution any more an essential ingredient of a retail sale than transmission? The point is that FERC's preemption theory is irrational and internally inconsistent.

FERC's second premise runs afoul of the FPA's legislative history, and the FPA's language, which (1) limits FERC's jurisdiction over transmission rates (§§ 205, 206(d) and 201(b)); (2) preserves pre-existing state regulation (§ 201(a)); and (3) safeguards state transmission programs (§ 212(h)). FERC's premise is also unrealistic and internally inconsistent.

3. The FPA's Plain Language Unequivocally Defeats FERC's Premise That Essentially All Retail Deliveries On The Interconnected Grid Are In Interstate Commerce

Because Congress safeguarded state regulation of retail transmissions "even where the energy moves in interstate commerce" (Senate Report 621 at 48), FERC's preemption of retail transmission service would be unlawful even if all transmissions were interstate. Further, because the FPA does not empower FERC to regulate retail transmissions, FERC would lack authority to preempt state regulation even if Congress had not safeguarded pre-existing state regulation of all aspects of retail transactions.

Finally, even if Congress had authorized FERC to regulate retail transmissions in interstate commerce, which it

has not done, FERC's preemption of all retail transmissions on the interconnected grid would still be unlawful because: (1) most retail electricity transactions involve generators and consumers that are not only in the same state, but in proximity (p. 45 n.28 infra); and (2) the FPA states that transmissions are not interstate if they are between buyers and sellers in the same state (§ 201(c)).

FERC's description of Florida Power & Light, 404 U.S. 453 (1972) and Jersey Central, 319 U.S. 61, 73 (1943), as holding that all interconnected retail transmissions are interstate is misplaced (States App. D-90-92). As discussed infra, neither case supports FERC's position.

a. Jersey Central's Holding That FERC May Regulate Stock Purchases By Public Utilities Does Not Support FERC's Position

In the late 1930's, Jersey Central Power & Light Company, without FERC's approval, sold securities to New Jersey Power. When the FERC directed both companies to show cause why FERC approval was not needed,[19] litigation followed and the Supreme Court eventually was asked to answer two questions: first, was Jersey Central a "public utility" under the FPA?; and second, was New Jersey Power's purchase subject to FERC's jurisdiction?[20]

---

[19] Section 204(a) prohibits public utilities from issuing securities without FERC approval. Section 203 requires FERC approval of stock sales by public utilities.

[20] Although § 203 of the FPA empowered FERC to review purchases of stock by public utilities, and New Jersey Power (as opposed to Jersey Central) was admittedly a public utility, a question remained whether § 201(a)'s admonition that federal

Question one, whether Jersey Central was a "public utility," turned on whether Jersey Central owned or operated facilities subject to the jurisdiction of the Commission (§ 201(e)). Inasmuch as § 201(b), as discussed above, assigned the Commission jurisdiction "over all facilities for . . . [interstate] transmission . . .," FERC's claim to review Jersey Central's financings came down to whether any Jersey Central transmission line carried any electric energy in interstate commerce.

Although no Jersey Central transmission line straddled a state line, the record showed that some energy generated by Jersey Central ultimately arrived in New York through an intervening company's transmission lines (319 U.S. at 63-64). Because Jersey Central's transmission lines, therefore, carried energy that was "transmitted from a state and consumed at any point outside thereof" [§ 201(c)], the Court held that Jersey Central's facilities transmitted energy in interstate commerce and Jersey Central was a public utility. 319 U.S. at 71-73.

The second issue was whether FERC's authority to review security purchases by public utilities applied to New Jersey Power. Noting that "although a company may be a public utility under subsection (e), all of its transactions do not thereby fall under the regulatory power of the Commission . . ., (319 U.S. at 73)" the Court asked whether FERC's § 203 power was nullified by § 201(a)'s preservation of pre-existing state regulation. Reasoning that § 201(a)'s "limitation is directed at generation, transmission and sale rather than the corporate financial arrangements of the utilities

---

regulation "extend only to those matters which are not subject to regulation by the state" barred FERC from regulating New Jersey Power's purchases from Jersey Central.

engaged in such production and distribution" (319 U.S. at 74, 75; emphasis added), the Court upheld FERC jurisdiction "to regulate the present transaction" (financing) (319 U.S. at 78; emphasis added).

The Court's analysis is instructive in several respects. First, the Court made it clear that all services of a "public utility" under § 201(e) are not FERC jurisdictional. 319 U.S. at 73. Thus, as indicated above, a company with transmission facilities that carried electricity in interstate commerce as well as intrastate commerce (see § 201(c)) would be a public utility, but FERC would not be able to regulate its retail transmission service (see 319 U.S. 74, 75) [§ 201(a)'s "limitation is directed at generation, transmission and sale . . .(emphasis added)"].

Second, in concluding that § 201(a)'s preservation of pre-existing state regulation did not negate Congress' authorization that FERC regulate purchases of stock by utilities, the Court explained how specific grants of authority (e.g., § 203 [reviews of purchases] and § 204 [sales]) should be read in the face of general denials of authority (§ 201(a)). As the Court indicated, Congress would not have spelled out FERC's authority to review purchases in § 203 if it had intended its § 201(a) denial of authority to nullify FERC's jurisdiction. Thus, § 201(a) gave way to § 203. Section 204(f)'s specific denial of FERC authority to review stock sales by public utilities where states reviewed stock sales, however, overrode the more general grant of authority in § 204(a) for FERC to review stock sales by public utilities.[21]

---

[21] Finally, the fact § 203 did not contain a limitation such as that found in § 204(f) demonstrated that Congress was willing to tolerate, not preemption, but dual regulation of stock purchases under which FERC controlled the purchase of the stock and the

The Court's analysis is applicable to this case because, like § 204(f)'s limitation of § 204(a)'s authorization regarding stock sales, § 201(c)'s definition of interstate transmissions limits § 201(b)'s authorization regarding transmissions. Reading from the general to the specific, § 205 assigns FERC rate jurisdiction over transmission service, but generally limits that jurisdiction to transmission "subject to the jurisdiction of the Commission." Section 201(b) specifically limits FERC's transmission jurisdiction to "transmission of electric energy in interstate commerce" and § 201(a) preserves state jurisdiction over retail transmissions.

Thus, while there was a tension to be resolved in Jersey Central (between § 203's specific grant of power and § 201(a)'s general denial of jurisdiction), there is harmony in this case between § 205's limitation of FERC's transmission jurisdiction, § 206(d)'s recognition that FERC's jurisdiction over transmission facilities is broader than its jurisdiction over transmission services, and § 201(a)'s denial of FERC authority to preempt pre-existing state regulation, which includes the transmission of electricity to end-users. Each provision rejects FERC's claim that it may regulate all transmissions.

Finally, Jersey Central reiterates that an analysis of whether a utility can be regulated -- which turns on whether it owns facilities that transmit any energy in interstate commerce -- differs dramatically from an analysis of whether FERC may regulate a specific utility service, such as retail transmission. In the case of determining the use of a utility's facilities, the question is whether some energy generated in one state is consumed in another. 319 U.S. at 68-73. In the case of determining whether a utility service can be regulated

---

New Jersey Board of Public Utility Commissioners controlled the sale.

by FERC, the question is: does the FPA clearly assign the specific service to FERC's bailiwick (id. at 73-78)?[22]

When state commissions, after Jersey Central, requested an amendment to the Federal Power Act to resolve any conceivable doubt over state jurisdiction, the FPC testified that an amendment was unnecessary because ". . . regulation of retail rates and local services is left to the states by the present Act even where the energy moves in interstate commerce." Hearings Before the Committee on Interstate and Foreign Commerce, House of Rep., 84th Cong., 1st Sess., on H.R. 2972, Testimony of FERC Chairman Smith (1947 Hearings on H.R. 2972) at 336; States App. N-14.[23] FERC's reliance on Jersey Central is misplaced.

---

[22] FERC's December 1942 Brief in Jersey Central implicitly acknowledged that utility lines are used for interstate and intrastate transmissions (pp. 22-23). This concession cuts directly against FERC's current claim that all retail transmission in interconnected lines is interstate (J.A. 349-50, States App. D-44, FERC Order 888 at 31,781; J.A. 391-92, States App. D-92, FERC Order 888 at 31,968-31,969; J.A. 593-95, States App. E-40-41, FERC Order 888-A at 30,339-40).

Further, while properly insisting that § 201(a)'s denial of FERC jurisdiction over matters regulated by the state had no relevance to whether FERC could assert jurisdiction over Jersey Central, FERC acknowledged that § 201(a) resolved ambiguities (p. 25) and "might be of moment when a particular regulation is questioned" (p. 28). As discussed above, § 201(a)'s denial of jurisdiction to FERC over matters regulated by the states is of significant moment in this case because FERC seeks to preempt the states' regulation of an essential element of retail service.

[23] To the extent it would have reversed the result of Jersey Central, the amendment could have denied FERC jurisdiction over most electric utilities.

b. Florida Power & Light's Holding That FERC Could Review Florida Power & Light's Books Does Not Support FERC's Position

In Florida Power & Light, the ninth largest utility in the country argued that it was not a "public utility" and, therefore, was not subject to FERC's regulation of its accounting practices.[24] In order to "require FP&L to follow the Commission's Uniform System of Accounts" (FERC Brief at 23; States App. O-9), FERC needed to show only that Florida Power & Light's transmission facilities carried one or more electrons that were generated in Florida and consumed in Georgia.[25] FERC assured the Court that it did not seek to regulate any Florida Power & Light service.[26] May 1971 Brief for the Federal Power Commission at 23, 24; States App. O-3-4.

---

[24] FPA § 301, 16 U.S.C. § 823, authorized FERC to review the books of public utilities.

[25] FERC described the issue as "whether interstate energy is present in a system or a particular portion of [FP&L's] system" (id. at 30; States App. O-9). The Court described the issue as whether "any FP&L power has reached Georgia, or FP&L makes use of any Georgia power, no matter how small the quantity . . ." (404 U.S. at 461 n.10; emphasis added).

[26] FERC's brief to the Supreme Court also conceded that FERC's rate jurisdiction over interstate sales was limited by Congress to sales at wholesale (§ 201(b)) and that FERC had "no authority over retail sales" (May 1971 Brief for the Federal Power Commission, id. at 21; States App. O-2). FERC added that the Federal Power Act was enacted "to extend federal authority only to those matters which could not effectively be controlled by the states." Id. at 20.

FERC offered two, alternative arguments in support of its position that Florida Power & Light's transmission facilities carried one or more electrons that were generated and consumed in different states. First, it hypothesized that all of the elements of the interconnected, interstate network, of which Florida Power & Light was a member, were locked in electromagnetic unity, that the slightest use of electricity in Florida Power & Light's service territory affected other states and that "this cause and effect relationship constitutes interstate transmission of electric energy" (FPC Brief, p. 25; States App. O-5). The Court neither approved nor rejected this argument.

Second, FERC relied on its staff's "tracing studies," which showed that some electrons generated in Florida Power & Light's transmission system, after commingling with electricity in intermediate utilities' lines, eventually made their way into Georgia (May 1971 Brief for the Federal Power Commission, pp. 32-37). Thus, as in Jersey Central, FERC pointed to record evidence that one or more electrons in the company's transmission lines were consumed in another state.

The Court determined that the FERC staff's tracing studies represented substantial evidence in support of FERC's position (404 U.S. at 464-465, 469). It, therefore, concluded that Florida Power & Light was subject to FERC jurisdiction. 404 U.S. at 469.

FERC's reliance on Florida Power & Light for preemptive power over all retail transmissions on the interconnected grid is baseless for several reasons. First, FERC did not argue in Florida Power & Light, and the Court's decision did not even remotely suggest, that all electrons transmitted by Florida Power & Light (or any other utility) crossed state lines. FERC's inductive expansion of

Florida Power & Light equates to an argument that if one human being has one or more white blood cells, then all blood cells of all human beings are exclusively white. Just as the existence of white blood cells in human beings does not render red blood cells nonexistent, the fact that there was substantial evidence in Florida Power & Light that one or more electrons in Florida Power & Light's transmission facilities crossed state lines does not suggest all electrons in all interconnected utilities cross state lines and are consumed in states other than where they are generated.

Second, FERC's reliance on Florida Power & Light is inconsistent with its description to Congress of its own Florida Power & Light decision. When Congress called hearings in response to FERC's Florida Power & Light decision, FERC Chairman White testified that FERC's assertion of jurisdiction over Florida Power & Light had no relevance to the jurisdiction of states over retail services (1967 Hearings before the Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce, 90th Cong., 1st Sess., Testimony of FERC Chairman Lee C. White, at 125; States App. H-15).

Third, FERC's use of Florida Power & Light as a preemption weapon is inconsistent with its implication to this Court that an affirmance of its order would not permit it to regulate retail matters. States App. O-2-4.

FERC was correct in its various decisions before Order 888, its sworn testimony to Congress in 1967 and its 1971 briefs to this Court in FP&L. Its reversal of position destroys any claim to deference that FERC could make for its reading of § 201(b) (see Point I). Food and Drug Administration v. Brown and Williamson Tobacco Company, 529 U.S. 120, ___, 120 S.Ct. 1291, 1313-15 (2000).

c. FERC's Reading Of Florida Power & Light And Jersey Central Renders Section 201(c) Nearly Nugatory

Section 201(c) provides that transmissions are in interstate commerce "if transmitted from a state and consumed at any point outside thereof." As indicated above, whether retail transmissions are in interstate commerce has significance only for the purpose of determining whether FERC has jurisdiction over the owner of the facilities used for the transmissions. Nonetheless, even if one assumes arguendo that states can only regulate intrastate retail transmissions, a premise defeated by Point B.1. supra, § 201(c)'s directive that transmissions from utilities to consumers in the same state are intrastate would still require an annulment of FERC's preemption order.

FERC's position, nonetheless, is that FP&L and Jersey Central render "interstate" all transmissions on lines connected to the national grid.[27] Thus, FERC implicitly claims the Court overrode § 201(c)'s unambiguous definition that transmissions are in interstate commerce only if the electrons they carry are consumed in a state other than that in which they are transmitted.[28] Florida Power & Light and

---

[27] In order to reconcile its position with § 201(c)'s definition of interstate transmission, FERC would have to show that essentially every electron used by a retail customer in each state (other than Hawaii, Texas and Alaska) is generated in a different state. No such showing could be reasonably attempted.

[28] Further, even if Congress had not avoided potential debate by enacting a definition of interstate transmission, FERC's apparent assumption that all energy transmitted on an integrated grid is a commingled stream of random electrons is incorrect. Irrespective of the location of the buyer and seller, most energy passes from

Jersey Central offer no support for the suggestion that the Court intended to negate § 201(c).

POINT III

FERC PREEMPTION OF RETAIL TRANSMISSION WOULD IMPEDE SOUND ENERGY POLICY

A competitive electric marketplace is best served by adequate generation supply and ample avenues for delivery. State agencies are responsible for the siting of generation (e.g., New York State Public Service Law Art. 10) and transmission facilities (e.g., New York State Public Service Law Art. 7). By defeating the states' ability to allow for capital recovery of new transmission facilities, FERC's preemption decision could impede the siting of new transmission lines, and thereby impair the states' competitive policies, which FERC supports (J.A. 348, States App. D-42, FERC Order 888 at 31,780).

The manner in which transmission lines are maintained affects not only the reliability of retail service, but customers' bills. For example, if a utility takes a transmission line out of service for maintenance during the business week, it may avoid paying overtime, but create transmission, or distribution, constraints that dramatically increase prices.

---

power plants to the retail customers who are first in line on transmission lines with suitable capacity. Corresponding energy movement in other parts of the grid has no significance. Nonetheless, even these indirect reactions do not occur in radial (direct line) delivery systems designed to serve retail load. See R. Sarikas, Introduction to Electrical Theory and Power Transmission, 70, 82 (1995); D. Fink & H. Beaty, Standard Handbook for Electrical Engineers, 2-4 (1987).

FERC is in no position to oversee the maintenance of transmission lines, yet by claiming power to preempt state regulation of the rates, terms and conditions of retail transmission service, it has potentially undermined the states' authority to do so.

Further, the reliability of the transmission system has been preserved for over six decades by federal/state cooperation. States with transmission systems that require local attention have acquired sufficient engineering resources to carry out this oversight. Regions with less complicated transmission paths, which lend themselves to one-size-fits-all modeling, have relied on industry self-regulation or FERC oversight. Order 888's preemption theory, again, undermines the authority of states to do what FERC cannot, and should not be asked to do, such as (a) supervising the coordination of the high voltage and low voltage arms of the delivery system; (b) requiring economically efficient system upgrades in response to local reliability requirements; (c) establishing and overseeing procedures for responding to transmission outages in a manner that assures safe and reliable service; and (d) seeking appropriate remedies when such procedures are not followed.

In preempting retail transmission rates, FERC has taken upon itself the responsibility for setting the depreciation charges that end-users will support through retail transmission rates. FERC is not in a position to assess the useful lives (and, therefore, the proper depreciation charges) for transmission lines throughout the nation. It is one thing for FERC to accept utilities' depreciation estimates for wholesale ratemaking purposes; it is another to impose such estimates on state regulators who have the resources to examine the utilities' estimates. See Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355 (1986)

[annulling a Federal Communications Commission order preempting the regulation of depreciation charges].

Further, as the Court has often indicated (e.g., Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989)), ratemaking entails a delicate balancing of ratepayer and shareholder interests, particularly with respect to retail rate regulation. This balancing affects millions of customers in various service classifications (residential, small business, industrial). One-size-fits-all ratemaking, by definition, omits such balancing.

Finally, FERC's preemption theory is self-defeating in that it discourages state regulatory agencies from unbundling[29] by diminishing the ratemaking jurisdiction of agencies that do so. It is irrational, contrary to sound energy policy and, as discussed in Points I and II, violative of the rule of law.

CONCLUSION

The 1935 Congress authorized FERC to regulate wholesale sales and interstate transmissions, but it denied FERC jurisdiction over matters subject to state regulation -- which included retail transmissions. While conceding that Congress did not envision unbundling (J.A. 594, States App. E-40; FERC Order 888-A at 30,339-40), FERC argues that "[t]oday's unbundled world" (id.) changes the retail/wholesale "jurisdictional lines" (J.A. 349-50, States App. D-44; FERC Order 888 at 31,781). If Congress did not envision unbundling, the sine qua non of FERC's preemption, then it could not have envisioned, much less intended, the preemption itself. Inasmuch as FERC is attempting to

[29] Cost of service studies needed for full unbundling can require significant resources.

preempt traditional, pre-existing state regulation without congressional authorization, its action should be annulled.

Respectfully submitted,

Lawrence G. Malone
Counsel of Record
General Counsel

Jonathan D. Feinberg
Diane T. Dean
Assistant Counsel
Public Service Commission of
the State of New York
Three Empire State Plaza
Albany, New York 12223-1350
(518) 474-2510

Counsel for Petitioners

April 2001

James Bradford Ramsay
General Counsel
Sharla Barklind
Assistant General Counsel
National Association of Regulatory
Utility Commissioners
1101 Vermont Avenue, Suite 200
Washington, D.C. 20005

Catherine D. Bedell
General Counsel
Richard Bellak
Associate General Counsel
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Alan G. Lance, Attorney General
Donald L. Howell, II, Deputy Attorney General
Idaho Public Utilities Commission
472 W. Washington Street
P.O. Box 83720
Boise, ID 83720-0074

John J. Farmer, Jr.
Attorney General, State of New Jersey
Helene S. Wallenstein, Senior Deputy
Attorney General
Attorney for New Jersey Board of
Public Utilities
124 Halsey Street, 5th Floor
P.O. Box 45029
Newark, NJ 07101

Jo Anne Sanford
North Carolina Utilities Commission
Robert P. Gruber, Public Staff, North Carolina
Utilities Commission
Gisele L. Rankin, Staff Attorney
4325 Mail Service Center
Raleigh, NC 27699-4325

William H. Chambliss, General Counsel
C. Meade Browder, Jr., Associate General Counsel
Virginia State Corporation Commission
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218

Christine O. Gregoire, Attorney General
William Berggren Collins, Senior Assistant
Attorney General
Robert D. Cedarbaum, Senior Counsel
(for the Washington Utilities and
Transportation Commission)
P.O. Box 40128
Olympia, WA 98504-0128

Harvey L. Reiter
(for the Vermont Department of Public Service)
Morrison & Hecker
1150 18th Street, N.W., Suite 800
Washington, D.C. 20036

Harry Ivey
(for the Wyoming Public Service Commission)
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002

Apr 19, 2001
CORRECTED COPY
(6) (7)
No. 00-568, No. 00-809
Supreme Court, U.S.
FILED
APR 19 2001
CLERK

IN THE

Supreme Court of the United States

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

CORRECTED COPY

STATE OF NEW YORK, *et al.*,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

BRIEF ON THE MERITS OF RESPONDENTS THE ELECTRICITY CONSUMERS RESOURCE COUNCIL, *ET AL.*

SARA D. SCHOTLAND
CLEARY, GOTTLIEB,
STEEN & HAMILTON
2000 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
202-974-1500

Counsel for The Electricity Consumers Resource Council, et al.

BEST AVAILABLE COPY

37 pp

QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission (FERC), which has jurisdiction over interstate transmission of electricity, is obliged to regulate such transmission for sales to retail customers on a bundled basis to remedy undue discrimination and to promote reliability of the interstate grid.

TABLE OF CONTENTS

QUESTION PRESENTED i
TABLE OF AUTHORITIES iii
OPINION BELOW 2
JURISDICTION 2
STATUTES AND REGULATIONS INVOLVED 2
STATEMENT 3
A. Interest Of Industrial Consumers 4
B. Statutory Background 7
C. Proceedings Below 7
ARGUMENT 8
I. To Assure A Reliable Interstate Transmission Grid, FERC Must Exercise Authority Over Bundled Retail Transmission 9
II. Unless FERC Exercises Jurisdiction Over All Interstate Transmission, Including Bundled Retail Transmission, Discrimination Will Persist 12
A. FERC Has A Duty To Address Anticompetitive Practices That Fall Within Its Jurisdiction 12
B. FERC Cannot Address Discrimination In Transmission Without Exercising Jurisdiction Over Transmission Associated With Bundled Retail Sales 14
CONCLUSION 20

TABLE OF AUTHORITIES

Cases

Alabama Power Co. v. FPC, 511 F.2d 383 (D.C. Cir. 1974) 12
Associated Gas Distribs. v. FERC, 824 F.2d 981 (D.C. Cir. 1987) 12
Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) 8
FPC v. Conway Corp., 426 U.S. 271 (1976) 12, 13
FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) 9
Gulf States Util. Co. v. FPC, 411 U.S. 747 (1973) 12
Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir. 2000) 7

Statutes

28 U.S.C. § 1254(1) 2
Federal Power Act, 16 U.S.C. §§ 792 *et seq.*
16 U.S.C. § 824 2
16 U.S.C. § 824(b) 7, 8
16 U.S.C. § 824(c) 9
16 U.S.C. § 824d 2
16 U.S.C. § 824d(b) 7
16 U.S.C. § 824e 2
16 U.S.C. § 824e(a) 7
16 U.S.C. § 824j 2
16 U.S.C. § 824k 2
16 U.S.C. § 824l 2
16 U.S.C. § 825l 2

Natural Gas Act, 15 U.S.C. §§717 *et seq*
15 U.S.C. § 717 2
15 U.S.C. § 717c.....2
15 U.S.C. § 717d 2

Legislative Materials

Electricity Deregulation: Hearing Before the Senate Committee on Energy and Natural Resources, 106th Cong. 183-88 (2000).....11
The Electricity Competition and Reliability Act: Hearing on H.R. 2944 Before the House Subcommittee on Energy and Power of the House Committee on Commerce, 106th Cong. 77-79 (1999) 10

Administrative Materials

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines after Wellhead Decontrol, Order No. 636, [1991-96 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶30,939 (1992) 17

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs ¶31,036 (1996).....*passim*

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-A, [Reg. Preambles] III F.E.R.C. Stats. & Regs. ¶31,048 (1997) .....*passim*

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities; Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats. & Regs. ¶32,514 (1995) .....*passim*

Miscellaneous Materials

"Reassessing Regulation in Light of Markets," Remarks of (former) Chairman James Hoecker, Mid-America Regulatory Commissioners Annual Meeting (June 12, 2000) 12, 17
Energy Information Administration, Department of Energy, Electric Power Annual 1999, Vol. 2 (2000).....4
Energy Information Administration, Department of Energy, Electric Sales and Revenue 1999 (2000).....4
Energy Information Administration, Department of Energy, Financial Statistics of Major U.S. Publicly Owned Electric Utilities 1999 (2000) 4
FERC Staff Investigation of Bulk Power Markets: Midwest Region (Nov. 2000).....19
Order Directing Staff Investigation, 92 FERC ¶ 61,160 (July 26, 2000) 18

Petition for a Rulemaking on Electric Power Industry Structure and Commercial Practices and Motion to Clarify or Reconsider Certain Open-Access Commercial Practices, FERC Docket No. RM98-5-000 (1998) 6

IN THE

Supreme Court of the United States

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

STATE OF NEW YORK, *et al.*,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

BRIEF ON THE MERITS OF RESPONDENT INDUSTRIAL CONSUMERS (THE ELECTRICITY CONSUMERS RESOURCE COUNCIL, AMERICAN IRON AND STEEL INSTITUTE, AND AMERICAN CHEMISTRY COUNCIL)

OPINION BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit is reported at 225 F.3d 667 (D.C. Cir. 2000), and reprinted at Petitioner's Appendix (Pet. App.) 3a to 121a. Federal Energy Regulatory Commission Order No. 888 is reported at F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21, 540 (1996). FERC's rehearing decisions, Order No. 888-A and Order No. 888-B, are reported respectively at III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997), and 81 F.E.R.C. ¶ 61,248, 62 Fed. Reg. 64,688 (1997). Relevant portions of FERC Orders Nos. 888 and 888-A and FERC's Notice of Proposed Rulemaking, F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,662 (1995), are reprinted at Pet. App. 125a to 654a.

JURISDICTION

The court of appeals entered its judgment on June 30, 2000, and issued its order denying a timely-filed motion for rehearing on August 22, 2000. This Court has jurisdiction under 28 U.S.C. § 1254(l).

STATUTES AND REGULATIONS INVOLVED

Sections 201, 205, 206, 211, 212, 213, and 313 of the Federal Power Act (FPA), 16 U.S.C. §§ 824, 824d, 824e, 824j, 824k, 824l and 825l, are reprinted in the Appendix at Pet. App. 652a to 681a.

Sections 1, 4, and 5 of the Natural Gas Act (NGA), 15 U.S.C. §§ 717, 717c, and 717d, are reprinted in the Appendix at Pet. App. 645a to 651a.

Relevant portions of FERC Orders Nos. 888 and 888-A are reprinted in the Appendix at Pet. App. 125a to 551a.

STATEMENT

FERC has found that vertically-integrated electric utilities have an incentive to deny use of the transmission wires that are an essential facility to deliver power to markets by providing transmission service to their own customers to the detriment of competing suppliers. In FERC Order No. 888, FERC found that transmission-owning utilities have an inherent incentive to discriminate, and have discriminated, against competing suppliers that are dependent on the utilities for transmission services. Pet. App. 213a-216a, 315a-331a. Based on this finding, FERC required utilities to file an "open access transmission tariff" (OATT) and to take transmission services for their own wholesale sales under the OATT pursuant to the same terms and conditions they offer to other users. Pet. App. 178a.[1] But FERC declined to apply this requirement to a utility's transmission services when the charge for power transmitted and distributed to retail customers is a single "bundled" charge that includes both the price of power and transmission. By declining to apply the OATT to transmission for bundled retail sales, FERC has failed to deal with the majority of transmissions that are the source of undue discrimination that FERC itself has found. Almost 60 percent of retail sales by investor-owned utilities and

---

[1] FERC applied this same requirement to unbundled retail sales, i.e., retail transactions in which the utility, either voluntarily or under compulsion at requirement of state law, states separate charges for the electric energy and for the service of transmitting the energy. Pet. App. 306a.

independent power producers are bundled.[2] Thus, FERC left the IOUs free to ignore the OATT, and discriminate in favor of their own retail customers, with respect to a very high percentage of the use of their transmission facilities.

FERC claimed in Order No. 888-A that it lacks jurisdiction to address discrimination in transmission associated with bundled retail sales. *See* Pet. App. 454a-456a. The court of appeals upheld FERC's discretion to determine that it lacked jurisdiction over interstate transmission for bundled retail sales.

A. Interest Of Industrial Consumers

The Electricity Consumers Resource Council (ELCON) is an association of industrial consumers of electricity organized to promote the development of

---

[2] In 1999, approximately 2.44 billion megawatt hours of electricity were sold at retail by FERC jurisdictional generators: 2.4 billion by investor-owned utilities (IOUs) plus 43 million by independent power producers (IPPs). *See* Energy Information Administration, United States Department of Energy (EIA), Financial Statistics of Major U.S. Publicly Owned Electric Utilities 1999, at 3 (2000); EIA, Electric Power Annual 1999, Vol. 2, at 87 (2000). At most, 915 million of these megawatt hours, or 37.5%, had previously been sold at wholesale. *Id.* (showing 545 million megawatt hours were available for resale by IOUs and 370 million megawatt hours were sold "to Utilities" by IPPs). About 76 million megawatt hours (3% of retail sales) were sold on an unbundled basis, with the remaining 97% sold on a bundled basis. *See* EIA, Electric Sales and Revenue 1999 at 3 (2000) (noting that total retail sales were generally made on a bundled basis); Electric Sales and Revenue 1999, at 245, 255 (2000) (showing transmissions of 76 million megawatt hours sold pursuant to "retail wheeling" programs, i.e., on an unbundled basis). In total, therefore, almost 60% (1.45 billion of 2.44 billion megawatt hours) of pertinent transmissions were bundled with retail sales.

coordinated and rational federal and state policies that will assure an adequate, reliable and efficient electricity supply for all users at competitive rates and prices. ELCON member companies produce a wide range of products, including: steel, aluminum, chemicals, petroleum, motor vehicles, industrial gases, machinery, glass, agricultural and food products, rubber, computer chips, paper and electronics. The member companies of ELCON consume approximately 5 percent of all electricity in the United States.

The American Iron and Steel Institute (AISI) is the principal trade association of the North American steel industry. Its member companies account for about 70 percent of the raw steel production in the United States. The steel industry is one of the most energy-intensive sectors in the United States; the cost of electricity for AISI members may constitute as much as 20 percent of the manufacturing cost of a steel mill product.

The American Chemistry Council (ACC) is a nonprofit trade association whose member companies represent more than ninety percent of the productive capacity of basic industrial chemicals in the United States. The manufacturing processes of many ACC member companies are highly energy-intensive. In addition, the chemical industry uses a substantial amount of self-generated electricity. Total electricity used by the industry, purchased plus self-generated, represents approximately 18 percent of industrial electricity consumption in the United States and approximately 6 percent of national electricity consumption.

Industrial Consumers are vitally concerned to have access to power supplies that are both reliable and low-cost. Recent events in California and other sections of the

country show the absolute urgency of maximizing the efficiency and reliability of the interstate grid. With respect to reliability, interruption in power supplies can have significant economic consequences. In the case of some industries, even momentary interruptions can yield losses of hundreds of thousands of dollars.

The cost of power represents an equally important consideration. Industrial Consumers must be able to enjoy the benefit of competition among available suppliers in electricity as with respect to other commodities and raw materials in order to be able to compete in international markets. It is essential to Industrial Consumers' own ability to compete that FERC eliminate discriminatory access to transmission facilities. Ending such discrimination is an essential condition to the development of competitive markets. Industrial Consumers, Enron, and other parties have long advocated that FERC conduct a rulemaking to assure that transmission providers are required to provide service to retail "native load" customers under the Order No. 888 OATT.[3] Discrimination will persist in the electric power industry until all transmission service, wholesale and retail, is subject to the same tariff. FERC's parsimonious view of its statutory mandate has prevented it from acting to assure

[3] On March 25, 1998, Enron, ELCON, and a coalition of power marketers and independent power producers filed a petition with FERC for a rulemaking that would require that all uses of the transmission service be subject to the OATT. The coalition asked FERC to unbundle transmission operationally from all merchant functions, including sales to captive native-loaded customers. *See* Petition for a Rulemaking on Electric Power Industry Structure and Commercial Practices and Motion to Clarify or Reconsider Certain Open-Access Commercial Practices, FERC Docket No. RM98-5-000 (1998). FERC never acted on the petition.

that all uses of the transmission grid are subject to the same set of rules.

B. Statutory Background

The FPA gives FERC jurisdiction over "the transmission of electric energy in interstate commerce" and "all facilities for such transmission." FPA § 201(b), 16 U.S.C. § 824(b). It also gives FERC jurisdiction over "the sale of electric energy at wholesale in interstate commerce." *Id.* Unlike its jurisdiction over the sale of electricity, FERC's jurisdiction over interstate "transmission" is not limited by the words "at wholesale." *See* Pet. App. 338a.

Section 205(b) of the FPA, 16 U.S.C. § 824d(b), bars any public utility, "with respect to any transmission or sale subject to the jurisdiction of the Commission," from "grant[ing] any undue preference or advantage to any person or subject[ing] any person to any undue prejudice or disadvantage" and requires each utility to file tariffs setting forth its "practices." Section 206(a), 16 U.S.C. § 824e(a), commands that if FERC determines that a practice is "unjust, unreasonable, unduly discriminatory or preferential," FERC must cure the discrimination and "determine the just and reasonable . . . practice . . . to be thereafter observed and in force, and shall fix the same by order."

C. Proceedings Below

In *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681, 687 (D.C. Cir. 2000), Pet. App. 8a-9a, 20a-21a, the court of appeals considered, on the one hand, the claim by state groups that FERC had exceeded its jurisdictional reach in Order No. 888 and, on the other hand,

the claim by Petitioner Enron that FERC interpreted its jurisdiction too narrowly. The State of New York and other parties contended that FERC has no jurisdiction over interstate transmission for any retail sales, even unbundled sales. The D.C. Circuit rejected this contention, holding that the Act confers jurisdiction over unbundled interstate transmission of electric energy whether it is then sold at wholesale or retail. Pet. App. 34a-35a.

With respect to Petitioner Enron's opposite argument that FERC has jurisdiction over bundled retail sales, the court acknowledged that it was a plausible reading of the FPA to construe transmission "bundled with generation and delivery services and sold to a consumer for a single charge as . . . transmission services in interstate commerce" within FERC's jurisdiction. Pet. App. 35a. [4] However, the court ruled that FERC's decision to decline jurisdiction over interstate transmission of electric energy for bundled retail sales was a "permissible policy choice" as to which FERC was entitled deference under *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984). Pet. App. 35a.

ARGUMENT

Section 201(b) of the FPA grants FERC jurisdiction over "the transmission of electric energy in interstate commerce and ... all facilities for such transmission." 16 U.S.C. § 824(b), Pet. App. 652a.[5] The

[4] Industrial Consumers endorse the legal argument presented by Petitioner Enron Power Marketing, Inc., in its Petition for Certiorari.

[5] The transmission of "electric energy in interstate commerce" is defined in the FPA as electric energy "transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States." 16 U.S.C. § 824(c), Pet. App. 653a.

statute contains no limitation on the Commission's jurisdiction over interstate transmission: only "local distribution" is reserved to the states. *See id.* FERC's jurisdiction over interstate transmission is not limited to wholesale transactions. *See FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972) (interpreting analogous provisions of the Natural Gas Act ("NGA"), 15 U.S.C. §§ 717, *et seq.*).

FERC's exercise of its authority over all interstate transmission is needed to assure a single set of rules for the road to govern interstate transmission—the highways by which electric power is distributed to market. The reliability of the transmission grid will be jeopardized if there is balkanization of regulatory control over bundled retail transmission between FERC and each individual state. FERC jurisdiction over all interstate transmission is also essential to avoid discrimination by transmission-owning utilities. Unless discrimination is eliminated with respect to the great majority of transmission associated with bundled retail sales, competitive power markets cannot develop.

I. To Assure A Reliable Interstate Transmission Grid, FERC Must Exercise Authority Over Bundled Retail Transmission

FERC exercise of its jurisdiction over bundled retail transmission is necessary to ensure the growth of competition in interstate power markets, and to prevent balkanization of the transmission grid. Federal jurisdiction over bundled retail transmission need not intrude on

appropriate areas of state regulation such as retail price regulation, certificating generation or local siting authority or the decision whether to adopt restructuring laws which may require utilities to divest generation or to institute retail customer choice. However, FERC exercise of its jurisdiction over transmission will allow consistency in determination of available transmission capacity, in congestion management, and in ascertaining the conditions under which transmission will be interrupted or curtailed.

A regime under which each state can set its own rules for operating the transmission system used to make bundled retail sales within that state is counterproductive to rational and coherent transmission regulation. The absence of a single regulator enables one state to favor transmission to its own residents, at the expense of its neighbors and at the expense of power destined for wholesale or unbundled retail transactions. The pernicious impact of allowing parochial and inconsistent administration of the interstate grid is intuitive and easily illustrated. In a time of congestion on an interstate highway, surely it would be intolerable for the state troopers of a given state to favor their own residents and require motorists with out-of-state license plates to exit the highway.[6] If anything, the consequences of chauvinistic state action are even more dire in electricity, as power does not flow simply from point to point but follows the path of least resistance. There are no side roads; power cannot be stored; and power inevitably

---

[6] *The Electricity Competition and Reliability Act: Hearing on H.R. 2944 Before the House Subcommittee on Energy and Power of the House Committee on Commerce*, 106th Cong. 77-79 (1999) (statement of FERC Commissioner William Massey).

moves through interstate transmission wires in an interconnected interstate grid.

The existing patchwork of inconsistent and outdated jurisdictional rules for this essential interstate delivery system, coupled with splintered network management, create obstacles and uncertainties that prevent development of a competitive market for electric power. If buyers and sellers lack confidence that electric power will be delivered reliably and on reasonable terms and conditions, they will not transact business.[7]

FERC Commissioner William Massey explained in testimony before the Senate Committee on Energy and Natural Resources:

> Electric power markets are inherently interstate in nature. The laws of physics, and hence power markets, do not respect state boundaries. In order to thrive, such markets must have an open, non-discriminatory, well-managed, and efficiently priced interstate transmission service that links buyers and sellers of power.

Electricity Deregulation: Hearing Before the Senate Committee on Energy and Natural Resources, 106th Cong. 183-88 (2000). Former FERC Chairman James Hoecker has similarly expressed concern that "divide[d] authority over reliability measures among states and between the states,

---

[7] Br. for the State Public Service Commissions In Opp'n, Jan. 26, 2001.

FERC and the industry threatens efficiency and indeed even reliability itself."[8]

FERC's failure to exercise its jurisdiction over bundled retail transmission threatens the orderly administration of the transmission grid and jeopardizes reliability of transmission service for all consumers.

II. Unless FERC Exercises Jurisdiction Over All Interstate Transmission, Including Bundled Retail Transmission, Discrimination Will Persist

A. FERC Has A Duty To Address Anticompetitive Practices That Fall Within Its Jurisdiction

In Order No. 888, FERC acknowledged that the FPA, like the NGA, "'fairly bristles' with concern for undue discrimination." Pet. App. 181a-182a, citing *Associated Gas Distribs. v. FERC*, 824 F.2d 981, 998 (D.C. Cir. 1987). *See also Gulf States Util. Co. v. FPC*, 411 U.S. 747, 758-59 (1973), *reh'g denied* 412 U.S. 944 (1973); *Alabama Power Co. v. FPC*, 511 F.2d 383 (D.C. Cir. 1974).

In *FPC v. Conway Corp.*, 426 U.S. 271 (1976), this Court considered whether the Federal Power Commission's (FPC's) authority, and responsibility, under §§ 205 and 206 of the FPA, extends to claims of discrimination between rates for two classes of service, only one of which is subject to the jurisdiction of the

---

[8] "Reassessing Regulation in Light of Markets," Remarks of (former) Chairman James Hoecker, Mid-America Regulatory Commissioners Annual Meeting, June 12, 2000, at http://www.ferc.fed.us.

Commission. The FPC had determined that it could not address price squeeze claims. This Court rejected the FPC's position as "untenable." *Id.* at 277. The FPC has "jurisdiction to consider the allegations of the company's wholesale customers that the proposed wholesale rates, which are within the Commission's jurisdiction, are discriminatory and noncompetitive when considered in relation to the company's retail rates, which are not within the jurisdiction of the Commission." *Id.* at 272-73. The Court observed:

> The Commission thus cannot so easily satisfy its obligation to eliminate unreasonable discriminations or put aside its duty to consider whether a proposed rate will have anticompetitive effects. *The exercise by the Commission of powers otherwise within its jurisdiction "clearly carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of interstate utility operations pursuant to . . . directives contained in §§ 205, 206. . . ."* *Gulf States Util. Co. v. FPC*, 411 U.S. 747, 758-759 (1973).

Id. at 278-279 (emphasis added).

In the case of electricity, as in natural gas, FERC has a statutory mandate to eliminate anticompetitive practices in interstate transmission.

B. FERC Cannot Address Discrimination In Transmission Without Exercising Jurisdiction Over Transmission Associated With Bundled Retail Sales

1. In The Order No. 888 Rulemaking, FERC Recognized The Potential For Discrimination Resulting From Excluding Bundled Retail Transmission From the OATT

FERC recognized in Order No. 888 that vertically-integrated utilities are motivated to discriminate in providing transmission access to their competitors:

> It is in the economic self-interest of transmission monopolists, particularly those with high-cost generation assets, to deny transmission or to offer transmission on a basis that is inferior to that which they provide themselves. The inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices.

Pet. App. 213a-214a.

In the notice of proposed rulemaking, the Commission recognized that if bundled retail service were not made subject to the OATT, then utilities will provide service

> . . . under two separate arrangements – an explicit wholesale transmission tariff filed at the Commission and an implicit retail transmission tariff governed by a state regulatory body. It also raises the possibility that the quality of transmission service for retail purposes will be superior to the quality of transmission service offered for wholesale purposes.

Promoting Wholesale Competition through Open Access Non-Discriminatory Transmission Services by Public Utilities, Notice of Proposed Rulemaking, IV F.E.R.C. ¶ 32,514 at 33,081-82 (1995), Pet. App. 634a. FERC found that "unduly discriminatory and anticompetitive practices exist today in the electric industry." Order No. 888, Pet. App. 213a. *See also* Order No. 888-A, Pet. App. 382a. "[T]he vast majority of utilities historically have declined to transport electric energy that would compete with their own sales or have offered access that is inferior to what they use for their own sales." Order No. 888-A, Pet. App. 436a-437a. Structural conditions in the industry "make it inevitable" that transmission owners will "act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors." Order No. 888, Pet. App. 213a-214a.

Because FERC has jurisdiction over all interstate transmission, and because FERC has found that utilities have the motive and the opportunity to discriminate in transmission services, the court of appeals erred in deferring to FERC's determination not to exercise its jurisdiction to remedy the discrimination that it found with respect to the majority of transmission uses: those bundled with retail sales.

2. The Same Authority That The Commission Exercised Under The NGA To Extend Nondiscriminatory Open Access to Natural Gas Retail Customers Is Available Under the FPA

Following introduction of open-access pipeline transportation in Order No. 436, discrimination persisted and lack of service comparability plagued gas markets:

> [T]he firm transportation embedded within the *pipelines' bundled, city-gate, firm sales service is superior* to the pipeline's open-access firm transportation service. This means that pipelines and other gas suppliers are not competing on an even basis for sales customers, even where firm transportation is available to move the gas sold by the pipelines' competitors.

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines after Wellhead Decontrol, Order No. 636, [1991-96 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 30,939 at 30,402 (emphasis added). Not. until FERC issued Order No. 636 and unbundled transportation completely from both the pipeline's wholesales and its direct retail sales was it able to achieve "an even basis for competition." *Id.*

Open access alone did not eliminate the incentives for pipelines to discriminate in favor of their own sales and against third-party shippers. Similarly, wholesale open-access electricity transmission does not establish comparability between the bundled transmission service that transmission-owning utilities use to serve their captive customers and the wholesale and unbundled retail transmission services that they provide to others. As Mr. Hoecker noted: "Recognizing the states' keen interest in ensuring that native load is not disadvantaged in the wholesale competition environment," FERC will "only be able to promote real competition to the extent that *all* uses of the grid and *all* transmission facilities are subject to the same non-discriminatory rules."[9]

With respect to the natural gas industry, FERC determined that in order to eliminate the incentive of a regulated transportation monopolist to discriminate in favor of its own and affiliated generation, it was necessary to make the merchant operation take transportation pursuant to rules identical to the rules that govern all other shippers. FERC's erroneous view of the parameters of its jurisdiction under the FPA is preventing the Commission from taking necessary

---

[9] Remarks of James Hoecker, *supra* (emphasis in original).

steps to eliminate discrimination in the electric power industry.

In July 2000, FERC commissioned a staff report on the state of regional bulk power markets due to FERC's grave concern with poorly-functioning markets. FERC observed that it was incumbent on the Commission to take steps to investigate malfunctioning markets and serious price volatility. *See* Order Directing Staff Investigation, 92 FERC ¶ 61,160 (July 26, 2000).

On November 1, 2000, FERC issued its report, "Investigation of Bulk Power Markets – Midwest Region." FERC's Staff Report on the Midwest markets recommends that FERC:

> [r]educe the advantages of network service over point-to-point service by requiring that native load be served under the same tariff provisions as other transmission services. Given that all transactions serve load of one sort or another, all load would be treated in the same manner. This would eliminate the current incentives that vertically integrated transmission owners have to favor their native load through the manner and method of calculating ATC [available transmission capacity] and handling interconnection requests. It would also restore confidence among market participants that transmission owners were not calling TLRs [a form of

> service curtailment] to favor native load, because they would no longer have the incentive to do so.[10]

The Staff Report goes on to find:

> [M]any vertically integrated transmission owners may have incentives to resist efforts to make this information [on available transmission capacity] transparent and standardized, including information on the manner in which "native load" is handled in making these calculations. . . . As a consequence, the Commission may wish to eliminate the native load exemption and have all transactions under the same tariff. Given that all transactions serve load of one sort or another, all load would be treated in the same manner. This would provide all transmission owners the proper incentives to make relevant information available.[11]

In Order No. 888-A, FERC stated that "[t]he record supports our conclusion that absent open access, undue discrimination will continue to be a fact of life in today's and tomorrow's electric power markets." Pet. App. 382a. The record at the time of the Order No. 888 rule and

---

[10] FERC, Staff Investigation of Bulk Power Markets: Midwest Region at 49 (Nov. 2000).

[11] *Id.* at 40.

the Agency's own reports since that date demonstrate that vertically integrated transmission-distribution utilities have a strong incentive to restrict the access of both wholesale and potential retail competitors to the transmission capacity that they control. Discrimination is ongoing and will persist until there is complete unbundling and consumers of all transmission services, wholesale and retail, take service pursuant to the same tariff at posted rates. FERC's unduly restrictive reading of its own jurisdiction prevents it from acting to remedy this discrimination.

CONCLUSION

The court of appeals' decision should be reversed.

Respectfully submitted,

Sara D. Schotland
Cleary, Gottlieb, Steen & Hamilton
2000 Pennsylvania Avenue, NW
Washington, D.C. 20006
(202) 974-1500

Counsel for The Electricity Consumers Resource Council, et al.

April 19, 2001

Apr 19, 2001

Supreme Court, U.S.
FILED
APR 19 2001

Nos. 00-568 and 00-809

IN THE
Supreme Court of the United States

NEW YORK, *et al.*,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF FOR RESPONDENT ELECTRIC POWER SUPPLY ASSOCIATION IN SUPPORT OF PETITIONER ENRON POWER MARKETING, INC.

JAMES VANR. SPRINGER
Counsel of Record
LARRY F. EISENSTAT
MICHAEL J. RUSTUM
STEVEN L. MILLER
DICKSTEIN SHAPIRO MORIN
& OSHINSKY LLP
2101 L Street, N.W.
Washington, D.C. 20037
(202) 785-9700

Counsel for Respondent Electric Power Supply Association

Wilson-Epes Printing Co., Inc. – (202) 789-0096 – Washington, D. C. 20001

BEST AVAILABLE COPY

RULE 29.6 STATEMENT

The Electric Power Supply Association has no parent corporation and no publicly held stock.

TABLE OF CONTENTS

	Page
RULE 29.6 STATEMENT	i
TABLE OF AUTHORITIES	iv
SUMMARY OF THE ARGUMENT	2
ARGUMENT	3
I. FERC'S DISAVOWAL OF ITS EXCLUSIVE JURISDICTION RELIES ON A MEANINGLESS DISTINCTION TO CREATE A REGULATORY GAP OVER THE MAJORITY OF INTERSTATE TRANSMISSION SERVICES	4
II. FERC'S STATUTORY INTERPRETATION PERPETUATES CONDITIONS THAT ALLOW TRANSMISSION-OWNING UTILITIES TO EXERCISE UNDUE DISCRIMINATION AGAINST OTHER USERS OF THE UTILITIES' INTERSTATE TRANSMISSION SERVICES	6
CONCLUSION	11

TABLE OF AUTHORITIES

CASES	Page
Phillips Petroleum v. Wisconsin, 347 U.S. 672 (1954)	6
STATUTES	
Federal Power Act, 16 U.S.C. §§ 792 *et seq.*16 U.S.C. § 824(d)	4
ADMINISTRATIVE MATERIALS	
Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888 F.E.R.C. Stats. & Regs., Regulations Preambles January 1991-June 1996, ¶ 31,036 (1996)	*passim*
Promoting Wholesale Competition Though Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888-A, III F.E.R.C. Stats. & Regs. ¶ 31,048 (1997)	2
Promoting Wholesale Competition Though Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888-B, 81 F.E.R.C. ¶ 61,248 (1997)	2
Open Access Same-Time Information System and Standards of Conduct, Order No. 889, F.E.R.C. Stats. & Regs., Regulations Preambles, ¶ 31,036 (1996)	9
Regional Transmission Organizations, Notice of Proposed Rulemaking, F.E.R.C. Stats. & Regs. ¶ 32,541 (1999)	7

IN THE

Supreme Court of the United States

Nos. 00-568 and 00-809

NEW YORK, *et al.*,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

---

BRIEF FOR RESPONDENT ELECTRIC POWER SUPPLY ASSOCIATION IN SUPPORT OF PETITIONER ENRON POWER MARKETING, INC.

The Electric Power Supply Association ("EPSA") is the national trade association representing competitive suppliers of electric power throughout the United States. EPSA's members are dependent upon transmission-owning electric utility companies for the interstate transmission services needed to deliver wholesale power to their customers for ultimate distribution to retail customers.

EPSA submits this brief in support of Petitioner Enron Power Marketing, Inc. ("Enron"), to bring to the Court's attention matter relevant to an understanding of the practical impacts of the jurisdictional issues in this case. In this brief, EPSA explains how the Federal Energy Regulatory Commission's ("FERC") failure to exercise jurisdiction under the Federal Power Act ("FPA") over interstate electric transmission bundled with retail sales of power—which constitutes the majority of interstate electrical transmissions—has resulted in a regulatory gap that gives vertically integrated electric utilities significant advantages over, and incentives to discriminate against, other interstate users of the utilities' transmission systems. EPSA incorporates herein the introductory sections of Petitioner Enron's brief.

SUMMARY OF THE ARGUMENT

Interstate electrical transmission bundled as part of a retail sale of electricity is, in every respect but for how it is marketed and billed to the consumer, exactly the same as any other interstate electrical transmission that FERC regulates. It should thus be subject to the same regulations and nondiscriminatory open access transmission provisions set forth in FERC Order Nos. 888, 888-A and 888-B (referred to collectively herein as "Order No. 888")[1] with respect to unbundled interstate transmissions of electrical energy.

[1] *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities*, Order No. 888 F.E.R.C. Stats. & Regs., Regulations Preambles January 1991-June 1996, ¶ 31,036 (1996); *Promoting Wholesale Competition Though Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities*, Order No. 888-A, III F.E.R.C. Stats. & Regs. ¶ 31,048 (1997); *Promoting Wholesale Competition Though Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities*, Order No. 888-B, 81 F.E.R.C. ¶ 61,248 (1997).

Indeed, it makes little sense for FERC to implement rules designed to promote nondiscriminatory open access to all users of the interstate electric transmission grid and then determine that the majority of interstate transmission use is not subject to those rules.

An examination of the practical consequences of FERC's choosing not to exercise jurisdiction over interstate transmission when bundled with retail sales highlights why the Court should overrule the Court of Appeals' affirmance of FERC's renunciation of comprehensive jurisdiction over interstate transmission. FERC's refusal to make interstate transmission bundled with retail sales subject to nondiscriminatory open access rules automatically allows utilities to discriminate in favor of the utilities' own sales, denying others equal access to interstate transmission. Because FERC's jurisdiction over interstate transmission is exclusive, its determination that it lacks jurisdiction over the majority of interstate transmission uses has created an unnecessary and unacceptable regulatory gap over the interstate transmission that a utility claims is used to serve retail customers. This absence of uniform governmental oversight has allowed public utilities to manipulate schedules and system dispatch to their own benefit without fear of discovery or serious reprisal.

ARGUMENT

FERC's decision creates a regulatory gap through which utilities can avoid government regulation and oversight over the bulk of their interstate transmission. A closer look at the practical nature and consequences of FERC's truncation of its exclusive jurisdiction to prevent undue preference or discrimination in the provision of all interstate transmission service confirms the error of that decision.

I. FERC'S DISAVOWAL OF ITS EXCLUSIVE JURISDICTION RELIES ON A MEANINGLESS DISTINCTION TO CREATE A REGULATORY GAP OVER THE MAJORITY OF INTERSTATE TRANSMISSION SERVICES.

Under Section 205 of the FPA,[2] Congress vested in FERC the exclusive authority to bar public utilities from granting any undue preference or advantage to any person with respect to interstate electric transmission service. Because FERC has determined that it lacks exclusive jurisdiction over transmission bundled with retail sales, there now is no regulatory supervision—either federal or state—to prevent undue discrimination or preference in the reservation and use of nearly two-thirds of the interstate electric transmission capacity in this country, which is used by utilities to serve retail customers.[3] FERC's creation of this regulatory gap is based upon the fallacy, to which the Court of Appeals deferred, that interstate transmission, when part of a retail sale and not billed to the customer as a separate service,

[2] 16 U.S.C. § 824(d).

[3] In 1999, 3.2 billion megawatts of electricity were sold at retail on a bundled basis. Energy Information Administration, United States Department of Energy, *Electric Sales and Revenue 1999* at 3 (2000) (hereinafter *Electric Sales and Revenue*). Of these, approximately 2.81 billion megawatt hours were sold at retail by FERC jurisdictional generators: 2.4 billion by investor-owned utilities and 410 million by independent power producers. *See* Energy Information Administration, United States Department of Energy, *Financial Statistics of Major U.S. Publicly Owned Electric Utilities 1999* at 3 (2000). At most, 988 million megawatt hours of that 2.81 billion megawatts, or 34.1 percent, was previously sold for resale. *Id.* And, only 76.2 million megawatt hours (2.4 percent of retail sales) were sold on an unbundled basis, with the remaining 97.6 percent sold on a bundled basis. *See Electric Sales and Revenue 1999* at 245, 255 (2000) (showing transmissions of 76 million megawatt hours sold pursuant to retail wheeling programs, *i.e.*, on an unbundled basis). In total, therefore, almost two-thirds (1.75 billion of 2.8 billion megawatt hours) of pertinent transmissions were bundled with retail sales.

ceases to exist as such, becoming instead merely part of a retail sale that is beyond the Commission's jurisdiction. This is a distinction without meaning, and it produces conditions under which load serving utilities serving—or purporting to serve—their own retail customers can freely discriminate against other interstate transmission users, including utilities from neighboring regions that require transmission access to deliver power purchased on behalf of their own bundled retail customers.

The bundled/unbundled distinction fails to recognize that the inherent nature of interstate transmission of electricity does not change merely because it is bundled for billing purposes as a component of a retail sale of electricity. A utility's use of interstate transmission on behalf of its retail customers has all the same physical characteristics, utilizes the same transmission facilities, and crosses the same interstate borders as all other interstate transmissions of electricity. The only difference is whether the utility labels transmission as a separate product.

For most of the prior century, the Commission's jurisdictional posture with respect to the transmission component of retail power service reflected the physical and commercial reality that transmission was used exclusively to deliver a bundled product to captive retail customers. That such transmission went unregulated was both pragmatic and understandable in view of the states' regulation of retail power sales and the near complete absence of wholesale competition. This is, however, an antiquated view. FERC's exercise of its exclusive jurisdiction can no longer lie dormant. Transmission services now are a separate and separable component of nearly every delivery of electric power and should be regulated consistent with FERC's exclusive jurisdiction and responsibility to prevent discrimination, which the states are unable to remedy.

Notwithstanding the fact that interstate transmission service is easily separated into a verifiable component of retail sales, FERC has renounced its exclusive jurisdiction over the interstate transmission component unless transmission-owning utilities—the very ones who benefit from discriminatorily controlling access to their transmission facilities—make the unlikely choice voluntarily to unbundle interstate transmission service from their retail electric sales, or are ordered to do so as part of a state electric restructuring program that would unbundle retail sales to allow customers to choose their own retail suppliers of electricity. FERC's action effectively permits the parochial business and regulatory interests of utilities and states to determine the scope of FERC's jurisdiction over interstate transmission and, consequently, FERC's authority to remedy undue discrimination through imposition of nondiscriminatory open access transmission.

Given that Congress has granted comprehensive and exclusive jurisdiction over interstate transmission to FERC, the agency's abdication of that authority is impermissible. Indeed, it is in direct conflict with this Court's holding in *Phillips Petroleum v. Wisconsin*, 347 U.S. 672 (1954), where the Court held that the jurisdiction of the Federal Power Commission was not intended to vary from state to state, depending upon the degree of state regulation and of state opposition to federal control.

II. FERC'S STATUTORY INTERPRETATION PERPETUATES CONDITIONS THAT ALLOW TRANSMISSION-OWNING UTILITIES TO EXERCISE UNDUE DISCRIMINATION AGAINST OTHER USERS OF THE UTILITIES' INTERSTATE TRANSMISSION SERVICES.

The Court of Appeals' affirmance of FERC's legal error improperly legitimizes FERC's refusal to guard against abuses in the use of interstate transmission and perpetuates conditions that allow transmission-owning public utilities to

discriminate in favor of their own power sales and against entities that are dependent upon those public utilities' transmission systems to deliver or receive electricity. The following examples illustrate certain discriminatory practices that transmission-owning utilities have employed and continue to employ against transmission-dependent members of EPSA in the absence of regulatory oversight of all interstate electrical transmission.[4]

Improperly Blocking Available Transfer Capacity By Overscheduling Transmission For Retail Loads: Not being subject to FERC's nondiscriminatory transmission access rules, transmission owning utilities with captive retail customers can "block" available transfer capability (*i.e.*, the capability of the physical transmission network to accommodate further commercial activity over and above its committed uses) across valuable transmission paths or segments of the interstate transmission grid. They do so by heavily reserving capacity for their own use over such segments, claiming that the transmission capacity is needed to serve their own retail customers, whether or not such a need exists. Regardless of whether such action is intentional or the result of inaccurate calculations of available transfer capability, the result is the same. By limiting the publicly available transfer capability over a particular transmission path, the utility can block transmission-dependent entities from acquiring or selling low-cost power over that same path, and thereby prevent others from competing with the utility for that low-cost power. For example, a utility can post no

---

[4] FERC, in *Regional Transmission Organizations*, Notice of Proposed Rulemaking, F.E.R.C. Stats. & Regs. ¶ 32,541, 33,709-10 (1999), discussed a Petition for Rulemaking (which EPSA supported) submitted in FERC Docket No. RM98-5-000 that set forth these and other examples of discriminatory treatment. FERC referenced this petition to highlight the need for further rulemaking to address ongoing discriminatory practices not cured by Order No. 888.

available transfer capability for a path traversing its system (A to B), thereby precluding a low-cost seller on one side of its system from selling power directly to a buyer on the other side. At the same time, however, the utility may post substantial available capacity from a point internal to its system to exit the system at point B, and may import the low-cost power from point A into its own system ostensibly for use to serve its retail load. This imported power can then be resold by the utility to the buyer at point B at a marked-up price insulated from the low-cost competition that would otherwise have occurred at point B.

Improper Avoidance of Costs: A transmission provider can purchase energy for peak service to its own retail load, schedule the import of that energy for the following day, and designate itself as the user of the energy for its retail load. This allows the transmission provider to pay no separate transmission charge to import the energy into its service territory. In the hourly market for the following day, the transmission provider or its marketing affiliate can sell the energy as "non-peak" to a neighboring service area and pay only a transmission charge for exporting that energy. Other transmission customers, however, would be prohibited from scheduling such power for a day ahead without charge, "parking" that power, and then deciding to transfer energy out in the hourly market. Rather, the other customers would have to pay for transmitting that power *into and out of* the initial transmission provider's system. During off-peak periods when a transmission provider is selling at wholesale the power it has paid nothing to import, its wholesale competitors are severely and unfairly disadvantaged. Under FERC's interpretation of the FPA, because utilities do not have to disclose their transmission for bundled retail service, this conduct is difficult, if not impossible to detect.

Failing To Make Accurate Disclosure Of Available Transfer Capability: Another consequence of FERC's jurisdictional determination is that utilities do not have to procure transmission on a comparable basis to their competitors, and therefore, do not have to report transmission reserved for their retail loads on the Open Access Same-Time Information System ("OASIS"; an internet-based transmission availability and scheduling system on which public utilities must publicly post transmission availability and transactions pursuant to Order No. 888's companion order, FERC Order No. 889 [5]). As a result, these utilities have no incentive to produce accurate calculations of available transfer capability. This can cause serious difficulties for suppliers attempting to schedule electricity sales across their transmission facilities. These reporting inaccuracies are cumulative in effect across geographic regions, often resulting in the underreporting of additional available transfer capability. This underreporting has serious consequences for suppliers and marketers that rely on OASIS information to schedule their power sales to buyers, at times forcing them to incur substantial losses due to the inability to schedule into regions where the amount of available capacity has been underreported.

These examples illustrate how FERC's abandonment of its jurisdiction and its concomitant limitation of applicability of Order No. 888 effectively nullify nondiscriminatory open access to interstate transmission. They also depict the opportunities for utilities to manipulate and frustrate wholesale competition and eliminate incentives for public utility transmission providers to accurately disclose surplus transmission capacity, particularly when transmission capacity is in high demand.

---

[5] *Open Access Same-Time Information System and Standards of Conduct*, Order No. 889, F.E.R.C. Stats. & Regs., Regulations Preambles, ¶ 31,036 (1996).

Moreover, FERC's determination that it lacks jurisdiction over bundled transmission makes redress of these discriminatory practices under FERC's general enforcement procedures nearly impossible. The lack of public access to a utility's retail load and transmission data creates a considerable informational void given that the majority of transmission reservations are for bundled retail customers. Without OASIS postings or any other regulatory oversight for the majority of transmissions, it is difficult, if not impossible, for FERC or any potential competitor to obtain information to prove that transmission owning utilities are engaging in discriminatory conduct by manipulating their scheduling and system dispatch to disadvantage wholesale transmissions (the only transmissions over which FERC lays claim). Moreover, the types of discriminatory actions described above occur within a period of minutes or hours. By the time FERC conceivably could take any action, a disadvantaged competitor's business opportunity would have passed.

Likewise, any complaints to a state utility commission would be limited to addressing a transmission-owning utility's manipulation of bundled retail sales over which the state would have jurisdiction. The states have no jurisdictional authority to order a utility to provide wholesale transmission service. Even if state jurisdiction could be established over a transmission dispute, there likely would be a preference for constituents served by the transmission-owning utility versus the interstate business interests of energy wholesalers, such as EPSA's members. Where a transmission-owning utility engages in discriminatory acts that restrict an electricity wholesaler from serving customers in a neighboring state, the issue is an interstate dispute that should be subject to FERC jurisdiction.

Put simply, without FERC regulation of all uses of interstate transmission, including the transmission component of bundled retail power sales, meaningful redress of

discrimination will remain difficult, if not impossible, to attain.

CONCLUSION

The Court of Appeals' decision should be reversed insofar as it affirms FERC's holding that its jurisdiction does not include interstate transmission bundled with local retail service.

Respectfully submitted,

JAMES VANR. SPRINGER
Counsel of Record
LARRY F. EISENSTAT
MICHAEL J. RUSTUM
STEVEN L. MILLER
DICKSTEIN SHAPIRO MORIN
& OSHINSKY LLP
2101 L Street, N.W.
Washington, D.C. 20037
(202) 785-9700
Counsel for Respondent Electric Power Supply Association

April 19, 2001

Nos. 00-568 & 00-809

Supreme Court, U.S.
FILED
MAY 10 2001
OFFICE OF THE CLERK

May 10, 2001

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF ENRON POWER MARKETING, INC. AS RESPONDENT IN NO. 00-568

JEFFREY D. WATKISS
BRACEWELL & PATTERSON, L.L.P.
2000 K Street, N.W.
Suite 500
Washington, D.C. 20006
(202) 828-5800

JOSEPH R. HARTSOE
SARAH NOVOSEL
ENRON CORP.
1775 I Street, N.W.
Washington, D.C. 20006
(202) 828-3360

LOUIS R. COHEN
Counsel of Record
JOSEPH E. KILLORY, JR.
JONATHAN J. FRANKEL
IJAY PALANSKY
MICHAEL PLOTNICK
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000

Counsel for Respondent Enron Power Marketing, Inc.

BEST AVAILABLE COPY

58 pp

QUESTION PRESENTED IN NO. 00-568

By Order filed February 26, 2001, this Court granted certiorari with respect to the following question:

Whether, given that Congress in 1935 stated that federal regulation extends "only to those matters which are not subject to regulation by the states" (Federal Power Act (FPA) § 201)), and the transmission of energy from generators to retail customers in the same state was then "subject to regulation by the states" (as it has been since 1935), may the Federal Energy Regulatory Commission (FERC) preempt state jurisdiction over such intrastate retail transmission of electric energy?

PARTIES TO THE PROCEEDING

The list of parties before the court of appeals is set forth at No. 00-809 Pet. App. 683a to 688a.

RULE 29.6 STATEMENT

Enron Corp. is the only publicly held company owning 10% or more of respondent Enron's stock. The following companies are the parent companies of respondent:

Enron Corp.

Enron North America Corp.

TABLE OF CONTENTS

Page

QUESTION PRESENTED IN NO. 00-568 ..... (i)

PARTIES TO THE PROCEEDING ii

RULE 29.6 STATEMENT iii

TABLE OF AUTHORITIES vii

OPINIONS BELOW 1

STATUTES AND RULES INVOLVED 2

STATEMENT 2

A. The Interstate Electric Transmission Grids 4

B. Statutory Background 6

C. The FERC Orders at Issue 11

D. Proceedings in the D.C. Circuit 13

SUMMARY OF ARGUMENT 14

ARGUMENT 16

I. FERC HAS JURISDICTION OVER ALL TRANSMISSIONS OF ELECTRIC ENERGY OVER THE INTERSTATE TRANSMISSION GRIDS. 17

A. All Transmissions of Electric Energy on the Interstate Grids Are "in Interstate Commerce" As Defined in the FPA. 18

B. FERC Has Jurisdiction Over Interstate Transmissions for Both Wholesale and Retail Sales, Notwithstanding the States' Jurisdiction Over the Retail Sales Themselves. 22

C. FERC's Jurisdiction Over Interstate Transmissions Is Not Limited by Section 201(b)'s Exclusion of Facilities Used in "Local Distribution." 28

TABLE OF CONTENTS — Continued

Page

II. FERC REGULATION OF ACCESS TO AND USAGE OF THE INTERSTATE GRIDS DOES NOT USURP ANY JURISDICTION THAT THE FPA RESERVED TO THE STATES. 32

A. FERC's Regulation of Access to and Usage of the Interstate Grids Does Not Encroach Upon State Regulation of Sales of Electric Energy at Retail. 33

1. FERC's Orders Do Not Regulate Sales of Energy at Retail. 34

2. The Matters FERC Has Regulated in Orders No. 888 and 888-A Are Not "Subject to Regulation by the States." 36

B. The Orders Under Review Expressly Provide for Continued State Regulation of Facilities Used in Local Distribution. 38

III. ONLY FERC CAN PROVIDE FOR NONDISCRIMINATORY OPEN ACCESS TO THE INTERSTATE GRIDS. 39

CONCLUSION 46

TABLE OF AUTHORITIES

CASES

Page(s)

AT&T Co. v. Central Office Telephone, Inc., 524 U.S. 214 (1998) 40

Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission, 461 U.S. 375 (1983) 19, 24, 25, 41, 44

Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) 23

Associated Gas Distributors v. FERC, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied sub nom., Interstate Natural Gas Ass'n of America v. FERC*, 485 U.S. 1006 (1988) 43

Board of Governors v. Dimension Financial Corp., 474 U.S. 361 (1986) 25

California v. Lo-Vaca Gathering Co., 379 U.S. 366 (1965) 20

Chemehuevi Tribe of Indians v. FPC, 420 U.S. 395 (1975) 21

Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) ..... *passim*

Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989) 35

FPC v. East Ohio Gas Co., 338 U.S. 464 (1950) .....

FPC v. Florida Power & Light Co., 404 U.S. 453 (1972) 30, 31, 38

FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) 23, 36, 42, 43

FPC v. Southern California Edison Co., 376 U.S. 205 (1964) 9, 20, 24, 29, 33

FPC v. Transcontinental Gas Pipe Line Corp., 365 U.S. 1 (1961) 43

Florida Power & Light Co., 37 F.P.C. 544 (1967) 5, 18, 19, 21

TABLE OF AUTHORITIES — Continued

Page(s)

Garcia v. United States, 469 U.S. 70 (1984) 25
Healy v. The Beer Institute, 491 U.S. 324 (1989) 43
Houston, East & West Texas Railway Co. v. United States, 234 U.S. 342 (1914) 37
Illinois Natural Gas Co. v. Central Illinois Public Service Co., 314 U.S. 498 (1942) 24
Jersey Central Power & Light Co. v. FPC, 319 U.S. 61 (1943) 33, 34
Mackey v. Lanier Collection Agency & Service, Inc., 486 U.S. 825 (1988) 32
Maislin Industries, U.S., Inc. v. Primary Steel, Inc., 497 U.S. 116 (1990) 23
Missouri v. Kansas Natural Gas Co., 265 U.S. 298 (1924) 24
Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953 (1986) 35
New England Power Co. v. New Hampshire, 455 U.S. 331 (1982) 19, 41
New York v. FERC, 121 S. Ct. 1185 (2001) 14
Northern States Power Co. v. FERC, 30 F.3d 177 (D.C. Cir. 1994) 19
Northern States Power Co. v. FERC, 176 F.3d 1090 (8th Cir. 1999), *cert. denied sub nom. Enron Power Marketing, Inc. v. Northern States Power Co.*, 528 U.S. 1182 (2000) 42
Panhandle Eastern Pipeline Co. v. Public Service Commission, 332 U.S. 507 (1947) 25
Pennsylvania Gas Co. v. Public Service Commission, 252 U.S. 23 (1920) 24, 25, 31
Pennsylvania v. West Virginia, 262 U.S. 553, *aff'd*, 263 U.S. 350 (1923) 41
Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927) 9, 24
Ratzlaf v. United States, 510 U.S. 135 (1994) 25

TABLE OF AUTHORITIES — Continued

Page(s)

Russello v. United States, 464 U.S. 16 (1983) 22
Tennessee Valley Authority v. Hill, 437 U.S. 153 (1978) 26
Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir. 2000) ..... *passim*
United States v. Price, 361 U.S. 304 (1960) 32
United States v. Public Utilities Commission, 345 U.S. 295 (1953) 33
Wyoming v. Oklahoma, 502 U.S. 437 (1992) 41

STATUTES

Natural Gas Act, 15 U.S.C. §§ 717 *et seq.*
15 U.S.C. § 717 ..... 2, 23, 30, 31
15 U.S.C. § 717c 2
15 U.S.C. § 717d 2
Federal Power Act, 16 U.S.C. §§ 792 *et seq.*
16 U.S.C. § 824 ..... *passim*
16 U.S.C. § 824a 8
16 U.S.C. § 824d 2, 9
16 U.S.C. § 824e 2, 9
16 U.S.C. § 824j 2, 37
16 U.S.C. § 824k 2, 37
16 U.S.C. § 824*l* 2
16 U.S.C. § 825*l* 2
Energy Policy Act of 1992, codified in pertinent part at 16 U.S.C. §§ 824j-824m 9
Public Utility Regulatory Policies Act of 1978, 16 U.S.C. §§ 2601 *et seq.* 9

LEGISLATIVE MATERIALS

S. Rep. No. 74-621 (1935) 26, 27, 44
S. Rep. No. 83-817 (1953) 31

TABLE OF AUTHORITIES — Continued

Page(s)

Memorandum of Oswald Ryan, General Counsel of the Federal Power Commission, and Dozier A. DeVane, Solicitor of the FPC, in *Public Utility Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Committee on Interstate Commerce*, 74th Cong. at 797 (1935) ..... 6, 7, 8 ,26

Public Utility Holding Cos., Hearings on H.R. 5423 Before the House Committee on Interstate and Foreign Commerce, 74th Cong. (1935) .. 7, 8, 24 ,26, 27

ADMINISTRATIVE CASES & MATERIALS

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996) .... *passim*

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-A, [Reg. Preambles] III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997) 2, 11, 12

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-B, 81 F.E.R.C. ¶ 61,248, 62 Fed. Reg. 64,688 (1997) 2

TABLE OF AUTHORITIES — Continued

Page(s)

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,622 (1995) 2, 10

Removing Obstacles to Increased Electric Generation and Natural Gas Supply in the Western United States, 94 F.E.R.C. ¶ 61,272 (2001) 45

San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services into Markets Operated by the California Independent System Operator and the California Power Exchange, 93 F.E.R.C. ¶ 61,121 (2001) 17

ARTICLES

Barrionuevo, Alexei & Gold, Russell, *Texas May Face a Glut of Electricity, But That Won't Aid Rest of U.S.*, Wall St. J., May 7, 2001, at A1 42

Claiborne, William, *Energy Forecasts for Summer: No Blackouts But Price Spikes*, Wash. Post, Apr. 30, 2001, at A3 40

Fialka, John J. & Davis, Bob, *Cheney Panel Considers Helping Utilities Expand Hydro Power Transmission Lines*, Wall St. J., May 3, 2001, at A2 .. 44

Kramer, Steven M. & Sumner, Bret A., *Electric Reliability in North America: Cross-Border Implications*, 14 Nat. Resources & Env't 81 (1999) 4

Sarikas, Robert H., *Introduction to Electrical Theory and Power Transmission* (1995) 20

TABLE OF AUTHORITIES — Continued

Page(s)

Smith, Rebecca & Emshwiller, John R., *Down to the Wire: Why California Isn't the Only Place Bracing for Electrical Shock*, Wall St. J., Apr. 26, 2001, at A1 40

Vactor, S.A. & Pickel, F.H., *Money, Power and Trade: What You Never Knew About the Western Energy Crisis*, 139 Pub. Util. Fort. 32 (2001) 17

OTHER AUTHORITIES

California State Auditor, Energy Deregulation: *The Benefits of Competition Were Undermined by Structural Flaws in the Market, Unsuccessful Oversight, and Uncontrollable Competitive Forces* (Mar. 2001) 17

Fink, D. & Beaty, H., *Standard Handbook for Electrical Engineers* (1987) 20

In The Supreme Court of the United States

Nos. 00-568 & 00-809

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF ENRON POWER MARKETING, INC. AS RESPONDENT IN NO. 00-568

OPINIONS BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit is reported at 225 F.3d 667 (D.C. Cir. 2000) and reprinted at No. 00-809 Pet. App. 3a to 121a. FERC Order No. 888 is reported at F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996). FERC's rehearing decisions, Order No. 888-A and Order No. 888-B,

are reported respectively at III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997), and 81 F.E.R.C. ¶ 61,248, 62 Fed. Reg. 64,688 (1997). Relevant portions of FERC Orders Nos. 888 and 888-A and FERC's Notice of Proposed Rulemaking (NOPR), F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,662 (1995), are reprinted at No. 00-809 Pet. App. 125a to 644a.

STATUTES AND RULES INVOLVED

Sections 201, 205, 206, 211, 212, 213, and 313 of the Federal Power Act (FPA), 16 U.S.C. §§ 824, 824d, 824e, 824j, 824k, 824*l* and 825*l*, are reprinted in the Appendix at No. 00-809 Pet. App. 652a to 681a.

Sections 1, 4, and 5 of the Natural Gas Act (NGA), 15 U.S.C. §§ 717, 717c, and 717d, are reprinted in the Appendix at No. 00-809 Pet. App. 645a to 651a.

Relevant portions of FERC Orders Nos. 888 and 888-A are reprinted in the Appendix at No. 00-809 Pet. App. 125a to 551a.

STATEMENT

The Federal Power Act (FPA) gives the Federal Energy Regulatory Commission (FERC) jurisdiction over all "transmission of electric energy in interstate commerce" without any stated limitation. 16 U.S.C. § 824(b)(1). In the orders under review, FERC exercised this jurisdiction to prevent vertically integrated public utilities from using their ownership of the nation's interconnected high-voltage transmission facilities to discriminate against competing power suppliers needing access to those facilities. FERC ordered each utility to file an open access transmission tariff (OATT) and to take transmission service for its own wholesales and (where a state requires or the utility voluntarily offers unbundled retail service) unbundled retail sales on the same terms of access and usage as its transmission-dependent competitors. In an era in which

competing suppliers and users must all use interconnected grids with limited capacity, federal regulation of the terms of access to and usage of the grids pursuant to the authority granted in the FPA is indispensable to workable, nondiscriminatory operation.

Petitioners State of New York et al. (New York) argue that FERC's orders are an unlawful "preemption" of state jurisdiction over retail sales of electricity. But FERC has not exercised any authority over retail sales. The fact that FERC's rules governing access to and usage of transmission facilities may affect the utility's cost for transmission, which is one of the costs a utility incurs to provide retail electric service, does not mean that FERC has regulated any aspect of retail sales or taken any jurisdiction from the states. FERC's regulation of interstate transmission leaves the states' jurisdiction over prices and other terms of retail sales of energy to end users entirely intact.

New York's legal premise, that FERC's transmission jurisdiction is limited to transmissions for "wholesales," reads into the FPA a limitation that Congress intentionally omitted. New York's further suggestion that transmissions on the Nation's two multi-state grids can be teased into separate (and separately regulatable) intrastate and interstate components ignores the fact that the grids are operated as synchronized, interstate networks, and the energy on these grids does not observe state borders. *Every* use by a user connected to a grid draws on every generator connected to that grid, wherever located. There is no such thing as a purely intrastate transmission on the interstate grids. To permit the forty-eight contiguous states to regulate "their" portions of the transmission grids as separate fiefdoms—and to permit them, in times of shortage, to hoard capacity for their in-state customers or prevent electricity from leaving the state—threatens the transmissibility of electric power throughout the country that federal regulation is designed to

promote as well as the competitive electricity markets that Congress sought to effectuate.

A. The Interstate Electric Transmission Grids

Three broad categories of facilities are used to provide electricity to end users. *Generation* facilities produce electric energy. Networks of high-voltage *transmission* lines carry electricity from the generators to local distribution points. After the electricity is stepped down to lower voltages, *local distribution* facilities deliver electricity from the distribution points to end users. Although the broad distinction between high-voltage transmission facilities and low-voltage local distribution facilities is generally understood and has long been recognized by this Court, *see Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 534-35 (1945), the exact demarcation is a matter of definition.

Today, the transmission facilities in every state (except Alaska, Hawaii, and part of Texas) interconnect into two large reticulated grids, the Eastern and Western Interconnections. *See* Steven M. Kramer & Bret A. Sumner, *Electric Reliability in North America: Cross-Border Implications*, 14 Nat. Resources & Env't 81, 82 (1999); *see also* Order No. 888 at 31,781, Pet. App. 305a n.541.[1] Most parts of these grids are owned by the vertically integrated public utilities that have traditionally provided electricity to their local customers on a regulated-monopoly basis. *See* Order No. 888 at 31,652, Pet. App. 172a. The utilities use these facilities for bulk transmissions of the electric energy that they sell either at wholesale (i.e., to entities that in turn resell) or at retail (i.e., to end users who receive electricity via the utilities' local distribution systems). Other power suppliers that compete against the vertically integrated

[1] All citations in this brief to "Pet. App." are to the Petitioner's Appendix filed with Enron's Petition for a Writ of Certiorari in No. 00-809.

utilities depend on the same transmission facilities to carry electricity to their customers.

Although customers and suppliers enter into bilateral contracts for the delivery of specific quantities of electricity, these contractual arrangements bear no resemblance to the physical behavior of electricity on the grids. A unit of electricity is not a discrete object that flows from a particular source to a particular buyer or user over a particular route, and a supplier generating electricity cannot prescribe the route over the grid that "its" electricity will follow. Each multi-state interconnection operates as a single pool of energy, into which generating facilities (wherever located) deposit electric energy, and from which customers (wherever located) draw it down.[2] Every connected use draws to some degree on every connected source, as the grid balances supply and use to ensure that the frequency of electric energy in the grid is maintained at a standard level, generally 60 cycles per second (or a multiple thereof). *See Florida Power & Light Co.*, 37 F.P.C. 544, 548, 564-65 (1967). "[A] load change at any point will have an effect on the instantaneous generation and frequency at every point on the interconnected system." *Id.* at 565. A sudden surge of use in Boston, or a downed high-voltage transmission line in New York, impacts electric operations in every state in the Eastern Interconnection. *See id.* at 548-50.

[2] In this respect, the electricity network is very different from, for example, the telephone network. When one telephone caller dials another, the switches in the telephone network establish a dedicated circuit between them that remains open for the length of the call, and all communications between the callers travel over this fixed open pathway. By contrast, when a generating utility contracts with an end user to deliver electricity, nothing travels on any path between them: the utility generates an additional amount of electric energy for the grid, and the end user withdraws a corresponding amount of electric energy from the grid. *See Florida Power & Light Co.*, 37 F.P.C. 544, 548, 567 (1967).

B. Statutory Background

Early in the Twentieth Century, because electricity could be produced in many places but could not be successfully transmitted over long distances without substantial losses, the electricity business was almost entirely local. *See Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681 (D.C. Cir. 2000), Pet. App. 9a; Order No. 888 at 31,639, Pet. App. 141a. Vertically integrated utilities, mostly confined to single states, each generated, transmitted, and distributed their own electricity, selling it to their retail customers on a bundled basis. "The industry consisted of independent, unassociated, local units [and] its piecemeal and planless development resulted in an uneconomic division of territory, wasteful overlapping of facilities, and lack of engineering and economic unity." Memorandum of Oswald Ryan, General Counsel of the Federal Power Commission (FPC), and Dozier A. DeVane, Solicitor of the FPC (Ryan-DeVane Memorandum), in *Public Utility Holding Company Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce*, 74th Cong. at 797 (1935).[3]

However, utilities gradually began to interconnect their generation and transmission facilities into regional networks. Interconnection permitted utilities to draw on more generation resources to meet variations in local demand and to achieve economies of scale by serving larger areas, allowing the utilities to enhance the reliability and profitability of their services. Increasingly, these networks crossed state lines; by 1933, roughly a dozen states either imported more than half their electricity from other states or exported more than half the power generated in-state to other states. *See* Ryan-DeVane Memorandum at 798 n.1.

Still, each of these regional networks grew in isolation. There was no coordinated planning of these networks,

[3] The Ryan-DeVane Memorandum summarizes the history of the industry up to 1935.

because no regulator exercised jurisdiction over interstate transmission: "Electricity crossing State lines is in a no-regulation land, unrestrained by the power of the State which may not constitutionally control it, and unrestrained by the power of the Federal Government, which has not attempted to control it." *Id.* at 798. As a result, transmission capacity *among* these regional networks was very inadequate. During World War I, for example, many regions of the country suffered power shortages because there was insufficient transmission capacity to import electricity from areas with adequate supplies. *See id.* (quoting War Department findings that "owing to lack of flexible and capacious interconnections between adjacent power systems it was virtually impossible to reduce this shortage . . . by taking advantage of the diversity factor and by releasing for active use part of the installed reserves which interconnection would have rendered safely available"). The consensus among federal policymakers in the mid-1930s was that inadequate transmission capacity threatened the health of the economy by preventing utilities from taking advantage of non-local lower-cost generation sources and by forcing them to maintain uneconomically high local reserves of generation capability. *See id.* at 798-800 (collecting sources).

The legislative hearings and debates leading to the adoption of the FPA in 1935 established the strong need for *federal* action to encourage and oversee the interconnection of transmission facilities. *See id.* at 800; *see also Public Utility Holding Cos.: Hearings on H.R. 5423 Before the House Comm. on Interstate and Foreign Commerce*, 74th Cong. at 2129 (1935) (*Hearings on H.R. 5423*) (statement of Dozier A. DeVane, Solicitor of the FPC) ("[J]ust as the original impetus to interconnection was given by the Government during the World War in requiring any company having excess capacity to transmit its surplus current to nearby territory in need of it, now the [federal] Government must take the lead if we are to achieve the unification desired in the new war upon economic waste and instability,

unemployment, and the progressive destruction of basic natural resources.") (internal quotations and citation omitted). As the General Counsel and Solicitor of the FPC then noted, "the vast saving to be accomplished by the proper coordination of power facilities, and the need for a centralized control of the coordination process furnishes a formidable basis for the exercise of congressional power." Ryan-DeVane Memorandum at 800; *see also Hearings on H.R. 5423*, at 384 (statement of Clyde L. Seavey, Commissioner of the FPC) (the FPA "is designed to secure coordination on a regional scale of the Nation's power resources").

In the FPA, Congress accordingly declared that "the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation . . . of that part of such business which consists of the transmission of electric energy in interstate commerce . . . is necessary in the public interest." 16 U.S.C. § 824(a). Congress gave FERC's predecessor, the FPC, jurisdiction over all "transmission of electric energy in interstate commerce" and all "facilities" used for such transmission. *Id.* § 824(b)(1). It defined electric energy "in interstate commerce" as energy "transmitted from a State and consumed at any point outside thereof." *Id.* § 824(c). The FPC was also given the authority to establish regional industry councils to coordinate the development of the grid and was empowered to order utilities to interconnect their transmission facilities with one another. *See id.* §§ 824a(a)-(b).

The FPA addressed other problems in the electric industry as well. Congress gave the FPC jurisdiction over "the sale of electric energy at wholesale in interstate commerce," a second area where there was a gap between state and federal authority. *Id.* § 824(b). The phrase "at wholesale" was applied to *sales* in order to provide a "bright line" between sales transactions subject to FPC jurisdiction

and sales transactions regulated by the states.[4] The qualifier "at wholesale" was not applied to *transmissions* in interstate commerce, all of which were made subject to the Commission's jurisdiction. *See* Order No. 888 at 31,969, Pet. App. 338a ("statute . . . makes no distinction between wholesale transmission and retail transmission").

In addition, the FPA commanded the FPC to remedy "undue discrimination." Specifically, section 205 of the FPA, 16 U.S.C. § 824d, bars any public utility, "with respect to any transmission or sale subject to the jurisdiction of the Commission," from "grant[ing] any undue preference or advantage to any person or subject[ing] any person to any undue prejudice or disadvantage," *id.*, and requires each utility to file schedules setting forth its "practices," *id.* § 824d(c). Section 206(a), 16 U.S.C. § 824e(a), directed the FPC, whenever it determined that a practice was "unjust, unreasonable, unduly discriminatory or preferential," to cure the discrimination: the FPC "shall determine the just and reasonable . . . practice . . . to be thereafter observed and in force, and shall fix the same by order."

The structure of the electric industry changed dramatically in the last decades of the Twentieth Century. In response to the energy crisis of the 1970s, Congress adopted two statutes—the Public Utility Regulatory Policies Act of 1978, 16 U.S.C. §§ 2601 *et seq.* (PURPA), and the Energy Policy Act of 1992 (EPAct), codified in pertinent part at 16

---

[4] *See FPC v. Southern California Edison Co.*, 376 U.S. 205, 211-12 (1964). As the Court there explained, with respect to sales, Congress was responding to the Court's decision in *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927), holding that the Commerce Clause barred states from regulating interstate wholesales. The wholesale/retail "bright line" served to distinguish jurisdictional from nonjurisdictional sales without case-by-case adjudication of Commerce Clause issues. There is no comparable distinction with respect to interstate transmissions, all of which are part of interstate commerce and have been subject to federal regulation since 1935. There is therefore no need for a "bright line" with respect to transmissions.

U.S.C. §§ 824j-824m—designed to encourage independent wholesale power suppliers to enter the market in competition with the traditional utilities. *See* Order No. 888 at 31,642-45, Pet. App. 147a-156a. These steps were extremely successful: by the early 1990s, "generating capacity added by independent producers exceeded capacity added by utilities." *Id.* at 31,643, Pet. App. 151a (citation omitted). Other competing suppliers also grew, including many traditional utilities that became electricity generators and marketers outside their "native" areas. *See id.* at 31,639, 31,641, Pet. App. 141a, 147a. Thus, the generation and marketing of power became the subjects of increasingly intense interstate competition. *See id.* at 31,635, 31,645-46, Pet. App. 131a-132a, 156a-157a.

With the boom in the number of competitive suppliers came a greatly increased demand for access to the interstate transmission grids. To reach their customers, the new suppliers of electric power needed to be able to purchase transmission services from their chief competitors, the traditional vertically integrated utilities that continued to own most segments of the interstate grids.[5] But grid owners had the incentive and the ability to cripple the new competitors by reserving their transmission facilities for their own transmissions and forcing competitors to make more expensive alternative transmission arrangements, or by manipulating the transmission "curtailment" process to bar competitors' power from the system during periods of system overload. FERC initially exercised its jurisdiction to regulate access to and usage of the interstate transmission grids by ordering transmission on a case-by-case basis under section 211 of the FPA, which authorizes FERC, upon application, to

[5] FERC found that "these entities needed transmission service in order to compete in electricity markets." Order No. 888 at 31,643, Pet. App. 150a. In order for there to be competitive power markets, "all wholesale buyers . . . must have equal access to the transmission grid." NOPR at 33,049, Pet. App. 558a.

order a transmission owner to provide transmission services to other suppliers and marketers. *See* Order No. 888 at 31,646, Pet. App. 157a-159a. FERC soon found, however, that the problem of discrimination was too widespread and entrenched for case-by-case resolution, and it began a rulemaking to address the problem on an industry-wide basis. *See id.* at 31,673, Pet. App. 191a-193a.

C. The FERC Orders at Issue

In Order No. 888 and, on rehearing, Order No. 888-A, FERC found that the traditional utilities that own much of the interstate transmission grids have inherent incentives to discriminate against other suppliers and are actually doing so. Structural characteristics in the industry "make it inevitable that [the transmission-owning utilities] will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors." Order No. 888 at 31,682, Pet. App. 214a; Order No. 888-A at 30,210, Pet. App. 436a. FERC found that vertically integrated utilities had in fact acted to harm competitors and competition, citing an "array of allegations and circumstances raised by customers in individual cases over the years." Order No. 888-A at 30,210, Pet. App. 435a. Examples in the record included refusals to transmit, dilatory tactics amounting to refusals to transmit, and refusals to offer comparable service. *See* Order No. 888 at 31,919-26, Pet. App. 315a-331a.

FERC recognized that, under sections 205 and 206 of the FPA, "it is our duty to eradicate unduly discriminatory practices." *Id.* at 31,682, Pet. App. 214a. In the current proceedings, FERC determined that a broad remedy was necessary because there was "more than sufficient reason to believe that transmission monopolists . . . will continue to engage in unduly discriminatory practices, unless we fashion a remedy to eliminate their ability and incentive to do so." *Id.* at 31,683, Pet. App. 216a-217a. FERC also held that it

had jurisdiction to adopt a remedy addressing interstate transmissions at wholesale and at retail when the retail service is unbundled: "Unlike our jurisdiction over *sales* of electric energy, which section 201 of the FPA specifically limits to sales at wholesale, the statute does *not* limit our *transmission* jurisdiction over public utilities to wholesale transmission." *Id.* at 31,781, Pet. App. 305a (emphasis added). "[W]hen a retail transaction is broken into two products that are sold separately," FERC held, "we believe the . . . unbundled transmission service involves *only* the provision of 'transmission in interstate commerce' which, under the FPA, is exclusively within the jurisdiction of the Commission." *Id.*, Pet. App. 306a.

The remedy FERC fashioned was "functional unbundling." FERC required every public utility to adopt and take service under an "open access transmission tariff" (OATT) containing terms to be applied to all transmissions for wholesale sales and *un*bundled retail sales. *Id.* at 31,654, 31,781, Pet. App. 178a, 306a. (Respondent Enron's separate petition in No. 00-809 challenges FERC's failure to apply the same requirement to transmissions for *bundled* retail sales.) The tariff covers conditions of access to and usage of the grid, such as reservation of capacity, scheduling of transmissions, and rules of priority when system conditions require curtailment of transmission. *See id.* at 31,721-44, 31,749-50, Pet. App. 254a-264a, 276a-278a; Order No. 888-A at 30,278-79, Pet. App. 456a-460a. FERC also required each utility to "state separate rates for wholesale generation, transmission, and ancillary services." Order No. 888 at 31,654, Pet. App. 178a. In sum, the OATT established that when a utility is selling at wholesale, or at retail on an unbundled basis, it must take transmission for itself on the same terms it offers to others.

At the same time, FERC acknowledged that its jurisdiction over high-voltage interstate transmission facilities did not extend to low-voltage local distribution

facilities, and it expressly noted state jurisdiction over the latter. *See id.* at 31,770-71, Pet. App. 281a-282a. FERC adopted a seven-factor test for distinguishing interstate transmission facilities from local distribution facilities, and it permitted the states to recommend precisely where to draw the jurisdictional line. *See id.* at 31,771, 31,783-84, Pet. App. 282a-283a, 311a-312a.

D. Proceedings in the D.C. Circuit

On petitions for review, the D.C. Circuit upheld FERC's orders against challenges that they exceeded FERC's jurisdiction. *See Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681, 687 (D.C. Cir. 2000) (*TAPS*), Pet. App. 8a-9a, 20a-21a. The State of New York and other parties contended that FERC has no jurisdiction over interstate transmission for *any* retail sales, even unbundled ones. The D.C. Circuit rejected this contention, holding that the FPA confers jurisdiction over unbundled interstate transmission of electric energy whether it is then sold at wholesale or retail. *See* Pet. App. 34a-35a. The court noted that "[t]he Supreme Court has interpreted the language in FPA § 201 regarding FERC's jurisdiction over transmissions in interstate commerce" and that it was "bound by the High Court's dictates to conclude that the FPA gives FERC the authority to regulate the transmissions at issue here, whether wholesale or retail." *Id.* at 34a. Even if this Court had been silent and the FPA were ambiguous, the D.C. Circuit held, "we would be hard pressed to conclude that FERC's interpretation of § 201[ ] as giving it jurisdiction over both wholesale and retail transmissions is unreasonable or impermissible." *Id.* at 35a.

The D.C. Circuit also upheld against state challenge FERC's seven-factor test for distinguishing between interstate transmission facilities and local distribution facilities, which it called a reasonable construction of the FPA. *Id.* at 38a-39a. New York petitioned for certiorari

from this ruling, No. 00-568, but the Court did not grant that portion of New York's petition. *New York v. FERC*, 121 S. Ct. 1185 (2001).

SUMMARY OF ARGUMENT

Since its adoption in 1935, the FPA has given FERC jurisdiction over interstate transmission of electricity and required it to eliminate undue discrimination in access to and usage of the facilities used to provide such transmission. Recent sweeping changes in the structure of the electric industry—the interconnection of virtually all transmission facilities in 47 states into two interstate networks, and the proliferation of competitive suppliers needing access to these grids—have increased both the amount of transmission subject to FERC's statutory jurisdiction and the need for FERC to exercise its authority. But there is no need to change the definition of FERC's jurisdiction adopted in 1935. New York's suggestion that FERC has reinterpreted the FPA to preempt state authority over retail electricity rates seriously mischaracterizes the orders under review and ignores the FPA's language. Moreover, state-by-state regulation of the nation's interstate grids would be a practical impossibility and a recipe for state-against-state discrimination.

I. Section 201(b) of the FPA gives FERC plenary authority over "the transmission of electric energy in interstate commerce," as well as the facilities used to provide such transmission, without any stated limitation. Since every act of consumption by a customer connected to an interstate grid draws on every generator on that grid, wherever located, *all* electricity on the interstate grids is "transmi[tted] . . . in interstate commerce" as a physical and legal matter. New York's claim that the uses of these grids can be teased into intrastate and interstate parts is unworkable. New York's further suggestion that FERC's jurisdiction is limited to "wholesale" transmissions reads language into the FPA that

is not there (and, indeed, that Congress consciously omitted); the state's snippets from the legislative record do not support its case and cannot override the language of the statute. Finally, amicus California's argument that there is no such thing as an interstate transmission facility—that every transmission over a grid for retail sale is state-jurisdictional "local distribution" regardless of how many states it crosses and how high the voltage at which it is carried—ignores the FPA's, and the orders', express distinction between transmission and distribution.

II. The states' argument that FERC has usurped traditional state regulatory authority has no merit. FERC's orders prescribe nondiscriminatory terms of access to and usage of the nation's interstate transmission grids, something the states have never done. The fact that these access and usage terms may affect the cost of one component of retail electric service does not mean that FERC has invaded the states' authority to set retail rates and terms; state ratemaking has always had to respect the costs that FERC approves for the facilities and services in its jurisdiction. The orders expressly disclaim any intention to regulate distribution facilities and contain a test specifically designed to distinguish between the proper spheres of federal and state regulators.

III. FERC adopted the orders after concluding that the vertically integrated utilities that own the transmission lines comprising the Nation's two interstate grids engaged in widespread discrimination against independent power suppliers, and that industry-wide open access tariffs were the only means for ending this discrimination. Individual states could not legally, and cannot practically, address the problem. State regulation would encounter formidable problems under the Commerce Clause if states attempted to prescribe detailed terms of access to and usage of the interstate grids. Moreover, state-by-state regulation of interstate transmission would, as promised by amicus

California, lead to attempts by individual states to reserve electricity and transmission capacity for their own customers at the expense of non-residents, threatening the free movement of electricity across the nation to the areas facing shortages. Finally, the interstate grids operate (and must be operated) as unified interstate wholes; it is unrealistic to expect separate regulation by each of the states to result in workable rules for access and use.

ARGUMENT

FERC found that the utilities that own and operate the facilities over which electricity is transmitted in interstate commerce engage in pervasive "undue discrimination" in favor of their own uses and against competing uses of their transmission facilities. To remedy this (in part), FERC ordered each owner or operator to publish an OATT and to take interstate transmission for itself on the same terms it offers to others. Petitioner New York argues that (i) transmissions over the interstate grid for retail sales are for the most part not physically in interstate commerce and (ii) the "bright line" separating federal jurisdiction over wholesale *sales* from state jurisdiction over retail *sales* also applies to *transmissions*, barring FERC from regulating transmissions for retail sales. Amicus California[6] argues that

[6] California represents its interest as amicus curiae as arising from the "electric utility disaster" that has befallen the Golden State, which California implies was caused by its ceding "to FERC regulatory jurisdiction over the [unbundled] retail transmission facilities of the State's three large investor-owned electric utilities." (Cal. Br. at 1.) Nothing could be further from the truth. It is widely recognized that, apart from the effects of low rainfall causing a shortage of hydroelectric generating capability, California's debacle was self-inflicted. Specifically, the California legislature and Public Utilities Commission caused the "disaster" by (1) requiring its utilities to purchase all of their power needs from two short-term exchanges at price-decontrolled wholesale prices and to resell that power to retail customers at regulated prices that turned out to be lower than the wholesale prices; and (2) doing this in a power market that had become supply constrained by the State's refusal to permit the development of new generating capability, despite the burgeoning demand of a booming economy. *See San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services into Markets Operated by the California Independent System Operator and the California Power Exchange*, 93 F.E.R.C. ¶ 61,121, at 61,351, 61,353, 61,360 (2001) (detailing disaster's causes); *see also* California State Auditor, *Energy Deregulation: The Benefits of Competition Were Undermined by Structural Flaws in the Market, Unsuccessful Oversight, and Uncontrollable Competitive Forces* 1-4 (Mar. 2001) (attributing California disaster to flawed state legislation and its implementation); S.A. Van Vactor & F.H. Pickel, *Money, Power and Trade: What You Never Knew About the Western Energy Crisis*, 139 Pub. Util. Fort. 32 (2001) (concluding that the California disaster was caused by poor planning, drought, excessive reliance on the spot market, and because "the richest state in the richest country in the world does not want to pay its bills").

(iii) interstate transmission, no matter the voltage or the number of states traversed, is part of "local distribution" if the ensuing transaction is at retail. All of these arguments are wrong: FERC may, only FERC can, and FERC must remedy the undue discrimination FERC found, so as to protect competition among suppliers and assure the efficient availability of electricity throughout the Nation.

I. FERC HAS JURISDICTION OVER ALL TRANSMISSIONS OF ELECTRIC ENERGY OVER THE INTERSTATE TRANSMISSION GRIDS.

New York argues that FERC lacks statutory jurisdiction to apply the OATT to transmissions for retail sales because (A) much of the electricity assertedly does not cross state lines and (B) in any event such transmissions are components of the retail sales and hence subject only to state regulation. Amicus California argues that (C) such transmissions are part of state-regulated "local distribution." All of these arguments ignore the plain language of the FPA and are wrong: no one quarrels with the states' exclusive jurisdiction over retail sales and over local distribution, but interstate

transmission is a distinct activity that has been clearly subject to federal regulation since 1935.

A. All Transmissions of Electric Energy on the Interstate Grids Are "in Interstate Commerce" As Defined in the FPA.

Section 201(c) of the FPA, 16 U.S.C. § 824(c), provides that electric energy is deemed to be transmitted "in interstate commerce" if it is "transmitted from a State and consumed at any point outside of the State." New York seizes upon this definition to argue (NY Br. at 43-45 & nn.27, 28) that FERC has jurisdiction over only the particular "electrons" that cross state lines. This argument, which is contrary to several consistent decisions of this Court, misunderstands both the science of electric energy and the definition in section 201(c).[7]

This Court has made it clear that whether electricity is consumed in a state other than the generating state depends on "an engineering and scientific, rather than a legalistic or governmental" test. *See Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 529 (1945) (*CL&P*). Under this test, all transmissions over an interstate grid are in interstate commerce because electric energy from every generator connected to an interstate grid becomes part of a pool of energy that serves all load requirements. "All of the electric energy produced by all the generating units [on an interconnected system] is delivered to the common coordinated and integrated modern transmission system from which all of the customers are supplied." *Florida Power & Light Co.*, 37 F.P.C. 544, 566 (1967). The operator of a particular generator cannot control the flow of "its" electricity to a particular end user and, conversely, a given

[7] California, eager to conflate interstate transmission with local distribution (as to which *see infra* pp. 28-31) insists exactly to the contrary. It expressly acknowledges the "technologically expansive scope of transmission in interstate commerce." (Cal. Br. at 11.)

user is served not by energy from a particular generator, either in or out of state, but by all generators connected to the grid. "[I]f a housewife in Atlanta on the Georgia system turns on a light, every generator on Florida's system almost instantly is caused to produce some quantity of additional electric energy which serves to maintain the balance in the interconnected system . . . ." *Id.* at 567-68, *quoted in FPC v. Florida Power & Light Co.*, 404 U.S. 453, 460 (1972) (*FP&L*).

This Court has recognized this "engineering and scientific" truth. In *CL&P*, the Court noted that the "[t]echnology of the business is such that if any part of a supply of electric energy comes from outside of a state it is, or may be, present in every connected distribution facility." 324 U.S. at 529. When end users are served by those distribution facilities connected to the interstate grid, they are, therefore, necessarily consuming energy from the pool served by all generators on the interstate grid. *See id.*

New York's argument that some of the energy flowing to a retail customer is identifiably intrastate, and hence beyond FERC's jurisdiction, is simply wrong. Regardless of the proximity of generator and user, if both are connected to an interstate grid it is not possible for the user to draw only on that generator without consuming any energy that originated out of state. *See Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 381 (1983). ("[I]t is difficult to say with any confidence that the power [an interconnected utility] provides to its [customers] at any particular moment originated entirely within the State."); *New England Power Co. v. New Hampshire*, 455 U.S. 331, 336 (1982) ("So long as the electricity produced at [a generator] continues to flow through [an interconnected] transmission network, it will be impossible to contain that electricity within [the generator's state] in any physical sense."); *Northern States Power Co. v. FERC*, 30 F.3d 177, 179 (D.C. Cir. 1994) ("There is no way to determine what

path electricity actually takes between two points or indeed whether the electricity at the point of delivery was ever at the point of origin."). None of the sources New York cites suggests otherwise.[8]

New York's converse suggestion (NY Br. at 43), based on the metaphor of red and white blood cells, that FERC's jurisdiction extends only to the particular electrons in each transmission that travel interstate, is contrary to this Court's interpretation of section 201 and is obviously unworkable. In *FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964), the Court deemed all sales of energy at issue "in interstate commerce" even though only some of the energy came from outside the state in which it was consumed. *See id.* at 208-09 (wholesale sale of energy generated in California, Nevada, and Arizona to the city of Colton, California, was "in interstate commerce"); *see also California v. Lo-Vaca Gathering Co.*, 379 U.S. 366 (1965) (sale of natural gas intended for use (and used in part) by the pipeline in its operations was within the FPC's wholesale jurisdiction because such gas commingled with other gas sold for resale). The identification and separate regulation of electrons from interstate sources is impossible: "There is a commingling of energy from different sources at a bus [a point of interconnection] with the result that the energy which flows away from such bus is so fully commingled as to consist of energy which has entered such bus both from

[8] The technical sources cited in footnote 28 of New York's brief do not support the contention that a customer's use of electric energy is or can be served exclusively by intrastate generation. The cited portion of *Introduction to Electrical Theory and Power Transmission* suggests only that a utility can generate the *amount* of energy necessary to offset the *amount* consumed by its native load, not that the energy consumed by the native load is somehow the "same" energy generated by the utility. *See* Robert H. Sarikas, *Introduction to Electrical Theory and Power Transmission*, 70, 82 (1995). New York's other citation, D. Fink & H. Beaty, *Standard Handbook for Electrical Engineers* 2-4 (1987), is unrelated to the point at issue.

interstate and intrastate sources." *FP&L*, 404 U.S. at 461-63; *see also Florida Power & Light Co.*, 37 F.P.C. at 550. To put this in the language of section 201(c), *whenever* a quantity of electric energy is "transmitted from [a generating facility in] a [connected] State," some part of the electric energy is "consumed at any point outside thereof . . . ." 16 U.S.C. § 824(c). Therefore, as Justice Douglas explained in dissent in *FP&L*, "every privately owned interconnected [transmission] facility in the United States . . . is within the FPC's jurisdiction." 404 U.S. at 471. Nothing in the words of section 201(c) requires that the definition of interstate transmission be applied, unworkably, to only the portion that is so consumed.[9]

Finally, the fact that all transmission over an interstate grid is "in interstate commerce" does not render section 201(c) "nugatory" as an original matter. (*See* NY Br. at 44-45.) Three states—Alaska, Hawaii, and part of Texas—remain unconnected to the interstate grids today, and many transmission facilities were not yet interconnected when the FPA was enacted to deal with the growing phenomenon of interconnection. *See supra* pp. 6-11. The transmissions falling within FERC's jurisdiction grew dramatically after 1935 because of increases in interconnection, not because of any change in the FPA or its interpretation.[10]

[9] California's brief directly contradicts New York on this point, stating "when any part of the electricity moves across state lines, transmission all the way to the retail customer is transmission in interstate commerce." (Cal. Br. at 11.)

[10] New York's reliance on *Chemehuevi Tribe of Indians v. FPC*, 420 U.S. 395 (1975), is thus misplaced. The argument in that case was that changes in policy and technology justified giving the statute a meaning fundamentally different than its language allowed. *Id.* at 422-23. Neither FERC nor Enron has made any such argument here.

B. FERC Has Jurisdiction Over Interstate Transmissions for Both Wholesale and Retail Sales, Notwithstanding the States' Jurisdiction Over the Retail Sales Themselves.

New York argues that the FPA draws a "bright line" between wholesale sales and retail sales and that every activity that serves a retail sale, including interstate transmission, is therefore reserved to the states' regulatory authority. New York says this is so regardless of whether the transmission service is sold for a separate charge or is bundled with the price of the energy at retail.[11] But this is a misreading of the plain language of the statute. FERC's jurisdiction over transmissions of energy in interstate commerce does not depend on its jurisdiction over wholesales or on how the transmitted electricity is sold; the "bright line," which provides a clear and workable rule for dividing federal and state jurisdiction over *sales*, has no application to interstate transmissions. This is made clear by the language of section 201(b), this Court's precedents, and the legislative history.

Section 201(b) of the FPA, 16 U.S.C. § 824(b), contains two separate grants of jurisdiction. The first gives FERC jurisdiction over all "transmission of electric energy in interstate commerce," and the second gives FERC jurisdiction over "the sale of electric energy at wholesale in interstate commerce." Although Congress limited FERC's jurisdiction over "sales" to those "at wholesale," it omitted that limitation from the grant of jurisdiction over "transmission." The different language in the two grants was intentional and must be given effect. *See Russello v. United States*, 464 U.S. 16, 23 (1983) ("where Congress includes

[11] Enron agrees with New York (NY Br. at 35-36) that whether the transmission charge and the electricity charge are bundled is a matter of bookkeeping and billing that does not affect the allocation of jurisdiction. Interstate transmission, however it is billed, is a separate activity subject to distinct regulatory jurisdiction.

particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion") (internal quotations and citation omitted).

This Court has interpreted the nearly identical parallel provision of the Natural Gas Act (NGA) to give FERC jurisdiction over all interstate transportation of natural gas, whether the transported gas is sold at wholesale or retail. Section 1(b) of the NGA grants jurisdiction over "[1] the transportation of natural gas in interstate commerce, [and] [2] the sale in interstate commerce of natural gas for resale." 15 U.S.C. § 717(b). In *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621 (1972), the Court explained that "[e]ach of the these is an independent grant of jurisdiction and, though the Act's application to 'sales' is limited to sales of interstate gas for resale, the Act applies to interstate 'transportation' regardless of whether the gas transported is ultimately sold retail or wholesale." 406 U.S. at 636. The Court has an "established practice of citing interchangeably decisions interpreting the pertinent sections of the two statutes." *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981). That practice should be applied in resolving this basic structural point, which is common to both statutes, the later of which (the NGA) was modeled on the earlier. Thus, even if the FPA language were not clear on its face, this Court's interpretation of the nearly identical NGA language would be controlling. *See Maislin Indus., U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116, 131 (1990) ("Once [this Court has] determined a statute's clear meaning, [it] adhere[s] to that determination under the doctrine of *stare decisis*, and we judge an agency's later interpretation of the statute against our prior determination of the statute's meaning.").

In fact, Congress rejected a proposal to rearrange the statute that was apparently intended to limit the FPC's

jurisdiction over transmissions to transmissions for wholesales. The National Association of Railroad and Utility Commissioners (NARUC, a predecessor of a petitioner in this case) proposed an amendment to the language that became section 201(b) that would have applied the "at wholesale" limitation to FERC's transmission jurisdiction: "The provisions of this title shall apply only to the transmission and sale at wholesale of electric energy in interstate commerce." *Hearings on H.R. 5423*, at 1660 (emphasis deleted). Congress did not accept this change and enacted the broader jurisdictional grant contained in section 201(b).

New York correctly states that the FPA drew a "bright line" between wholesale and retail sales. But none of the cases cited by New York suggests that this bright line applies to interstate *transmissions*. *See Public Util. Comm'n v. Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927) (state could not regulate "sale" of electric energy by Rhode Island company to Massachusetts company for resale); *Pennsylvania Gas Co. v. Public Serv. Comm'n*, 252 U.S. 23, 28 (1920) (state could regulate retail "sale" of interstate gas to local customers); *Missouri v. Kansas Natural Gas Co.*, 265 U.S. 298, 310 (1924) (regulation of "sale" of gas to retail customers, not "transportation"). An important doctrine arising out of these cases was "that the retail *sale* . . . was subject to state regulation" even if the commodity had been transmitted in interstate commerce, *see Arkansas Elec.*, 461 U.S. at 377 (emphasis added), but none of the cases suggests the need for a "bright line" dividing interstate transmissions.[12]

---

[12] New York cites (NY Br. at 29) *Southern California Edison*, 376 U.S. 205, but that case and the cases cited therein hold only that the state may regulate rates for local retail sales, not that FERC's jurisdiction over the transmission of electric energy (or the transportation of natural gas) is limited to wholesale transmission (or transportation). *See Illinois Natural Gas Co. v. Central Illinois Pub. Serv. Co.*, 314 U.S. 498, 504-05 (1942); *Panhandle E. Pipeline Co. v. Pub. Serv. Comm'n*, 332 U.S. 507, 517 (1947).

This is consistent with the reason for the bright line: to make it easy to ascertain where interstate commerce would be deemed to end, thereby avoiding a case-by-case evaluation of out-of-state and in-state interests in particular sales. Any retail sale was to be deemed subject to state jurisdiction, even though the electricity had been transmitted (and perhaps previously sold) in interstate commerce. *See Arkansas Elec.*, 461 U.S. at 375-77; *Pennsylvania Gas*, 252 U.S. at 28. But this bright line has no logical application to transmission, because all interstate transmissions are by definition in interstate commerce; the line that needs drawing is, instead, between transmission and local distribution. *See infra* pp. 28-31.[13]

New York tries to override the clear language of the FPA by selectively citing legislative history. Of course, the Court does "not resort to legislative history to cloud a statutory text that is clear." *Ratzlaf v. United States*, 510 U.S. 135, 147-148 (1994).[14] In any event, the legislative

---

[13] It made sense to give the FERC jurisdiction over all interstate transmissions because there is no physical distinction between interstate transmissions that serve wholesale and retail sales. The terms of sale are matters of contract. The transmissions, whether for wholesale or retail, compete for the use of the interstate grids, and it is that competition for usage that FERC has sought to regulate by mandating that an "open access" tariff be filed by all owners and operators of the facilities. FERC's important objective, as shown *infra* pp. 39-44, can only be accomplished by federal regulation, and Congress built into the FPA the jurisdiction over interstate transmissions necessary to enable FERC to do so.

[14] *See also Board of Governors v. Dimension Fin. Corp.*, 474 U.S. 361, 374 (1986) ("Invocation of the 'plain purpose' of legislation at the expense of the terms of the statute itself takes no account of the processes of compromise and . . . prevents the effectuation of congressional intent."); *Garcia v. United States*, 469 U.S. 70, 78 (1984) ("We are not willing to narrow the plain meaning of even a criminal statute on the basis of a gestalt judgment as to what Congress probably intended.");

history specifically discussing jurisdiction over interstate transmission clearly indicates that plenary FERC jurisdiction was a separate purpose of the FPA.[15] By 1935, the fledgling development of regional interstate electric power systems had "outgrown the States as to the . . . transmission of power, not the distribution." *See* Ryan-DeVane Memorandum at 798. "Electricity crossing State lines [was] in a no-regulation land, unrestrained by the power of the State which may not constitutionally control it, and unrestrained by the power of the Federal Government, which ha[d] not attempted to control it." *Id.* at 797. Congress enacted the FPA to establish federal regulation over the "uncontrolled and uncoordinated . . . transmission of electricity . . . [which] obstruct[ed] the free flow of electric energy in interstate commerce," *id.* at 800, and to encourage the further development of coordinated interstate grids, *see id.* ("the need for a centralized control of the coordination process furnishes a formidable basis for the exercise of congressional power provided in title II of the present bill").

The passages from the legislative record that New York cites discuss the retail/wholesale distinction only in the context of jurisdiction over sales; they do not address jurisdiction over transmission.[16] For example, the 1935

Tennessee Valley Auth. v. Hill, 437 U.S. 153, 184 n.29 (1978) ("When confronted with a statute which is plain and unambiguous on its face, we ordinarily do not look to legislative history as a guide to its meaning").

[15] Contrary to New York's suggestion, the FPA was enacted to do more than create federal authority to set wholesale rates: "I do not have to tell the members of this committee that the actual fixing of [wholesale] rates is but a small part of the regulation sought to be accomplished by this bill." *Hearings on H.R. 5423*, at 2170 (DeVane testimony); *see also* S. Rep. No. 74-621, at 17 (1935) (explaining that the purpose of the FPA was to fill not only the "Attleboro gap," but also to reach "[o]ther features of this interstate utility business that are equally immune from State control either legally or practically").

[16] The same is true of amicus California's discussion of legislative history. For example, California cites Solicitor DeVane's statement (Cal. Br. at 10-11): "The bill does not give the Commission jurisdiction over energy that is transmitted in interstate commerce by a particular company and sold by that company to consumers." The statement was made in a discussion of jurisdiction over retail and wholesale sales rates. When read in context, it is clear that Solicitor DeVane's statement simply distinguished between the FPC's authority to set wholesale sales rates and the states' authority to set retail sales rates, even when the energy sold at retail was "transmitted in interstate commerce." DeVane's comment does not suggest any limit on FERC's jurisdiction over the transmission of electric energy in interstate commerce.

Senate Report's discussion of the exclusions from federal jurisdiction, cited by New York (NY Br. at 23), focuses on the "retail sale of . . . energy in local distribution." S. Rep. No. 74-621, at 48 (1935). FPC Solicitor DeVane's much-cited comments contain considerable discussion in very general terms about the preservation of state authority, but none of his comments about jurisdictional boundaries suggests a limit on FERC's authority to regulate the rates, terms, and conditions of the transmission of electric energy in interstate commerce. *See Hearings on H.R. 5423*, at 497-98 (discussing limits on "retail" rates in the context of a discussion on the "retail sale" of electric energy). As for the few citations that do discuss transmission, New York either cites the legislative record out of context or, occasionally, misquotes it entirely. For example, New York twice mischaracterizes, by leaving off the final clause, the same statement of Solicitor DeVane about federal jurisdiction over transmission facilities. (*See* NY Br. at 22, 33.) He actually said that federal jurisdiction did not extend to "jurisdiction . . . over facilities used in local distribution or the transmission facilities that are used in connection with such local distribution *unless they are also part of the facilities that are used in interstate commerce.*" *Hearings on H.R. 5423*, at 548 (emphasis added). Leaving out the "unless"

clause dramatically changes the meaning, which is entirely consistent with section 201(b).[17]

C. FERC's Jurisdiction Over Interstate Transmissions Is Not Limited by Section 201(b)'s Exclusion of Facilities Used in "Local Distribution."

The FPA excludes from FERC's jurisdiction "facilities used in local distribution." 16 U.S.C. § 824(b). Amicus California makes the novel argument (Cal. Br. at 8 *et passim*) that *all* conveyance of electricity, from a generator wherever located, over facilities of any character, at whatever voltage, and regardless of state boundaries, is actually "local distribution" if the only sale is to a retail customer. According to California, "local distribution" is "a subset of . . . transmission in interstate commerce." (*Id.* at 8.) A transmission at high voltage over the interstate grid from generation facilities in New York to a distribution point in Ohio and thence to retail customers would all be "local distribution" unless there was an intervening wholesale. This argument, under which the local distribution exception would swallow most of FERC's jurisdiction over transmission, is contrary to the statute and this Court's established understanding of what it means.

The FPA makes it quite clear that "transmission" and "local distribution" are distinct activities. Section 201(b)

[17] New York argues that in earlier briefs to this Court and before Congress FERC has taken the position now urged by New York. All of the examples noted by New York, however, merely confirm FERC's recognition of state jurisdiction over retail sales and the local distribution of electric energy; in none does FERC deny or limit its own jurisdiction over interstate transmissions. For example, New York claims (NY Br. at 28) that in a December 1944 brief the FPC "conceded that the states regulated *all aspects* of retail transactions" (emphasis added), but the brief in fact acknowledges only that states have jurisdiction over the rates for "*sale* to the ultimate consumer." FPC's December 1944 Brief in *CL&P* at 28 (emphasis added).

says, "The Commission shall have jurisdiction over [1] all facilities for [interstate] transmission . . . but shall not have jurisdiction . . . over [2] facilities used in local distribution or [3] only for the transmission of electric energy in intrastate commerce." The statute is quite evidently using "transmission" and "local distribution" to mean different things. Moreover, California's view would prove too much: by California's definition, *all* transmission facilities are "used in local distribution" (at least some of the time) and hence beyond FERC's jurisdiction. If Congress actually meant, as California contends, to exclude all interstate transmissions for retail sales, it could have said so much more directly.

This Court has previously observed that there is a clear distinction between "transmission" and "local distribution" facilities (although the exact location of the line between them has been a matter of some specific disputes). In *CL&P*, on which California relies, the issue came down to whether the transformer facilities used in "the process of reducing energy from high voltage to low voltage in subdividing it to serve ultimate consumers," 324 U.S. at 534, were "transmission" facilities or "local distribution" facilities. The Court had no difficulty with the general distinction between the two:

> [T]ransmission . . . extends from the generator, where generation is complete to the point where the function of conveyance in bulk over a distance, which is the essential characteristic of 'transmission,' is completed and the process of subdividing the energy to serve ultimate consumers, which is the characteristic of 'local distribution,' is begun.

Id. at 533 (citations omitted). The Court instructed the court of appeals to remand the case to the FPC to determine on which side of the line the particular transformer facilities at issue fell. *Id.* at 534-36; *see also Southern California Edison*, 376 U.S. at 210 n.6 ("Whether facilities are used in

local distribution . . . involves a question of fact to be decided by the FPC as an original matter.").[18] The Court's reasoning and the result in *CL&P* make it clear that "transmission" and "local distribution" are essentially different activities.

The Court has drawn a similar distinction under the parallel provision of the NGA. Section 1(b) of the NGA gives FERC jurisdiction over the "transportation of natural gas in interstate commerce," but not over "the local distribution of natural gas . . . to the facilities used for such distribution . . . ." 15 U.S.C. § 717(b). In *FPC v. East Ohio Gas Co.*, 338 U.S. 464 (1950), the utility argued, as California does here, that all of its facilities used to transport gas to its retail customers were facilities for local distribution, exempt from federal jurisdiction even if used to transport gas in interstate commerce. *See id.* at 469-70. The Court rejected this "strained" interpretation, noting that it would exempt every pipeline owned by a vertically integrated utility and used to serve its retail customers. *Id.* at 470-71. The Court held that Congress intended by the language of the statute to create a clear distinction between the two types of facilities—"transportation" facilities carrying gas at high pressure and "local distribution" facilities carrying gas at reduced pressures to local users—even when both types of facilities are being used to serve a utility's own retail customers. *See id.*

---

[18] Contrary to California's argument (Cal. Br. at 18-19), the Court's n.6 in *Southern California Edison* does not suggest that any facility "used" in retail service is *ipso facto* a "local distribution" facility. The Court merely noted that the FPC had found, in a particular instance, that certain facilities were *not* engaged in local distribution because they were used to serve wholesale customers. That FPC reasoning makes perfect sense and does not imply that, conversely, all facilities used to serve retail customers are local distribution rather than transmission facilities. On the contrary, the Court made clear that the line between "transmission" and "local distribution" facilities is to be determined by the expertise of the agency, applied to the particular facts of each case, and is not a simple bright line between wholesale and retail.

California asserts (Cal. Br. at 23-24 & n.16) that *CL&P* casts doubt on the reasoning of *East Ohio Gas*. But both cases recognize distinctions—indeed, roughly parallel distinctions—between facilities used to carry a commodity in bulk over long distances and facilities used for local distribution to customers. *Compare East Ohio Gas*, 338 U.S. at 470-71 *with CL&P*, 324 U.S. at 533-34. Both cases concerned which side of the line particular intermediate facilities fell on, and the Court held in *CL&P* that the analysis of particular gas facilities in *East Ohio Gas* did not control the analysis of particular electric facilities in *CL&P*. *East Ohio Gas* is also not, as California argues (Cal. Br. at 24 & n.16), inconsistent with the (much earlier, pre-NGA) decision in *Pennsylvania Gas*, 252 U.S. 23. *Pennsylvania Gas* held only that the states had authority to regulate retail "sales" because they were a matter of local concern, *see id.* at 28; it did not hold that states have the power to regulate interstate transmissions for those sales. To the extent Congress "adopted" *Pennsylvania Gas* in the FPA, it did so by leaving retail "sales" jurisdiction to the states.

Congress later overturned the outcome in *East Ohio Gas* by amending the NGA to add section 1(c), 15 U.S.C. § 717(c), which now exempts from federal regulation an entity that receives gas at or within the boundaries of a state if all of the gas is used within the same state. This section, known as the Hinshaw Amendment, which has no parallel in the FPA, does not alter the distinction between transportation of gas (or transmission of electricity) and local distribution. It merely implements an overriding policy that gas companies engaged entirely in in-state activities should be subject only to state regulation. There was inserted into the Senate Report on this legislation the phrase "as always has been intended," *see* S. Rep. No. 83-817, at 1-2 (1953), but this does not retroactively alter the meaning of the NGA's original language, particularly the language with respect to the distinction between transportation and local distribution, which was not changed. *See Mackey v. Lanier Collection*

Agency & Serv., Inc., 486 U.S. 825, 839 (1988) (opinion of "later Congress as to the meaning of a law enacted 10 years earlier does not control the issue"); *United States v. Price*, 361 U.S. 304, 313 (1960) ("the views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one").

II. FERC REGULATION OF ACCESS TO AND USAGE OF THE INTERSTATE GRIDS DOES NOT USURP ANY JURISDICTION THAT THE FPA RESERVED TO THE STATES.

The Declaration of policy in section 201(a) of the Federal Power Act provides:

> Federal regulation of . . . the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

16 U.S.C. § 824(a). Following this declaration, section 201(b) gives FERC jurisdiction over the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce "but . . . not [over] any other sale of electric energy" and not over "facilities used in local distribution." 16 U.S.C. § 824(b). New York contends that Orders 888 and 888-A, insofar as they regulate transmissions of electric energy for retail sales, encroach upon state authority to regulate such sales. Amicus California contends that interstate transmission facilities become "local distribution" facilities when used for transmission of energy for retail sales and the orders therefore violate the states' reserved right to regulate local distribution.

Both of these arguments are wrong. FERC's exercise of its authority to regulate the terms and conditions of interstate

transmissions, an authority expressly granted by the statute, sets conditions that the states may be required to take into account in regulating retail sales, just as they must take into account FERC-fixed wholesale prices, but it does not usurp state regulation of rates for retail sales as such, or any state authority over retail sales. And FERC has made it entirely clear that it has not attempted to regulate local distribution facilities.

A. FERC's Regulation of Access to and Usage of the Interstate Grids Does Not Encroach Upon State Regulation of Sales of Electric Energy at Retail.

New York places far more weight on the Declaration of Policy in section 201(a) than it can properly bear. The section declares that *federal* regulation of interstate transmission of electric energy is "necessary in the public interest." To the extent that this policy is limited by reference to matters "subject to regulation by the states," the Court has made it clear that this general policy limitation yields to the specific grants of jurisdiction elsewhere in the statute. *See Southern California Edison*, 376 U.S. at 215 ("Section 201(b) embodies a clear grant of power, and we have held that [section] 201(a) was merely a 'policy declaration . . . of great generality. It cannot nullify a clear and specific grant of jurisdiction, even if the particular grant seems inconsistent with the broadly expressed purpose.'") (quoting *CL&P*, 324 U.S. at 527); *United States v. Public Utilities Comm'n*, 345 U.S. 295, 310-11 (1953) ("[Section] 201(a) was originally drafted as a declaration of 'policy,' and . . . [i]t cannot nullify a clear and specific grant of jurisdiction . . . .").[19] FERC's orders have not encroached on any jurisdiction granted or reserved to the states by the FPA.

---

[19] New York's reliance (NY Br. at 11, 28, 37-41) on *Jersey Central Power & Light Co. v. FPC*, 319 U.S. 61 (1943), for the proposition that section 201(a) grants the states jurisdiction over interstate transmission of electric energy for sale at retail is incorrect. *Jersey Central* merely noted

1. *FERC's Orders Do Not Regulate Sales of Energy at Retail.*

FERC's orders do not purport to regulate any aspect of the terms and conditions on which any utility sells electric energy at retail. *See* Order No. 888 at 31,635-36, Pet. App. 131a-134a (describing main aspects of the order). FERC's orders deal with terms of access to and usage of the interstate grids. The orders respond to findings of pervasive undue discrimination by vertically integrated utilities against competing power suppliers. The OATT was designed to level the playing field by requiring transmission owners to take their transmission on the same terms they offered their competitors, including access, curtailment policies, service priority ("firm" versus "non-firm" service), price, and service options and flexibility.[20]

FERC's regulation of access to and usage of the interstate grids to remedy undue discrimination is not regulation of retail sales. New York argues that because the OATT covers rates charged by transmission owners for interstate transmission service, and because the rate for the interstate transmission service is a component cost that the state must take into account in establishing the charges to retail customers for electricity, the OATT regulates the sale of energy at retail. (*See* NY Br. at 7-8, 11-12, 28-33.) But

---

that the policy set forth in section 201(a) had no application to the provisions of the FPA dealing with "corporate financial arrangements" and was properly considered in connection with the interpretation of the FPA provisions dealing with generation, transmission, and sale. *See id.* at 74-75. *Jersey Central* did not opine about the effect of section 201(a) with respect to generation, transmission, and sale, and did not hold that section 201(a) preserved any transmission jurisdiction to the states.

[20] Contrary to the impression that might be gained from New York's brief, the orders are not concerned exclusively, or even primarily, with transmission *charges*. Their central concern is terms of access and usage. *See TAPS*, Pet. App. 8a ("open access is the essence of Order[] 888"). *See infra* pp. 39-40.

the amounts that a local utility must or may charge its retail customers, the manner in which these amounts are presented on a retail bill, whether customers will be allowed to choose among energy suppliers, and all of the other terms and conditions of retail service remain matters wholly within the authority of each state.[21] To be sure, the states are not free to ignore FERC-established costs and conditions of interstate transmission insofar as these, under state law, affect retail charges. State rate regulation, if designed to allow the utility to recover its costs, must respect the rates set in tariffs filed with FERC for components of electric service that are within FERC's jurisdiction. *See Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 969-70 (1986). But the fact that the utility must pay FERC-filed charges for some of the component costs it incurs, and that the state must recognize this, does not make the federal government a regulator of retail rates any more than does the Federal Communications Commission's regulation of the long-distance charges paid by utilities in the course of doing business.

The situation parallels the allocation of jurisdiction over wholesale and retail rates. FERC has undisputed jurisdiction over the former, and the states have undisputed jurisdiction over the latter. A FERC-filed wholesale rate for power establishes a cost component for a utility that obtains power as a buyer at wholesale at that rate. In such situations, the state is not at liberty, in setting retail rates based on a utility's costs, to ignore the FERC-filed wholesale rate. As this Court explained in *Nantahala*, in setting the retail rate, the state regulator must "recognize a FERC-approved [wholesale] price as a reasonable cost for purposes of retail ratemaking." *Id.* at 973. But the fact that FERC establishes wholesale rates that the states are required to honor in setting retail rates does not mean that FERC is itself regulating retail sales. This

---

[21] This authority is of course subject to the constitutional rights of the regulated utilities. *See Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989).

principle applies equally to interstate transmissions, which like purchases at wholesale, are necessary components of electricity service at retail. As New York acknowledges (NY Br. at 9), all that Order No. 888 requires is that "the states that have separately identified the commodity . . . must incorporate FERC's transmission rate into the non-commodity . . . portion of the retail bill."[22]

In requiring a tariff setting forth terms and conditions for transmissions in interstate commerce, FERC has exercised only its own proper jurisdiction. Any resulting effect on state regulation of retail rates is not a usurpation but a consequence of a proper exercise of federal authority.

2. *The Matters FERC Has Regulated in Orders No. 888 and 888-A Are Not "Subject to Regulation by the States."*

New York also argues that because the states have always regulated all aspects of the sale of electricity at retail, and because interstate transmission costs are one component that must be taken into account in setting charges to the retail customer, jurisdiction over interstate transmission is reserved to the states under section 201(a). (*See* NY Br. at 11-12, 27-28.) But the states have never regulated competitive access to and usage of the interstate grids. The need for such regulation did not arise in its present form until the 1980s, with the birth of competition among suppliers of electricity.

---

[22] The Court has reached a similar conclusion under the NGA. In *LP&L*, the Court held that similar regulation by the FPC of access to and usage of interstate natural gas transportation facilities, pursuant to section 1(b) of the NGA, did not constitute retail ratemaking, and fell squarely within the FPC's jurisdiction over interstate transportation. *See* 406 U.S. at 637-38 ("[Section] 1(b) withheld from FPC only *rate-setting* authority with respect to direct [i.e., retail] sales. Curtailment regulations are not *rate-setting* regulations but regulations of the 'transportation' of natural gas and thus within FPC jurisdiction under the opening sentence of § 1(b) that 'the provisions of this Act shall apply to the transportation of natural gas in interstate commerce.'").

No form of regulation in which the states have ever engaged, or in which the FPA permits them to engage, would enable the states to provide for nondiscriminatory access to the interstate grids or for interstate transmission service on fair and equal terms for all users.

That such regulation was within the proper scope of federal power was implicitly recognized in the EPAct of 1992. In that legislation, to help address the access problems plaguing the system, Congress amended section 211 of the FPA, 16 U.S.C. § 824j, to authorize FERC to order utilities on a case by case basis to "wheel" power for other users over their interstate transmission facilities. The broader actions taken in the orders resulted from FERC's determination that a case-by-case approach was not sufficient to remedy the pervasive undue discrimination it had found. *See* Order No. 888 at 31,646-47, 31,673, Pet. App. 157a-159a, 191a-193a. FERC noted that its authority under section 206 to remedy undue discrimination was unaffected by the amendment of section 211. *See* 16 U.S.C. § 824k(e) (savings provision stating that section 211 "shall not be construed as limiting or impairing any authority of the Commission under any other provision of [the FPA]"); Order No. 888 at 31,673, Pet. App. 192a (section 211 "left unaltered the authorities and obligations of the Commission under sections 205 and 206 . . . to remedy undue discrimination"). Traditional state regulation of retail sales and local distribution facilities had no way of dealing with the access and usage issues that Order No. 888 addressed; FERC's orders are qualitatively unlike anything the states have ever done.[23]

---

[23] New York's reliance (NY Br. at 20-21, 25) on FPA legislative history discussing the *Shreveport Rate Cases* to support its assertion that the FPA reserved jurisdiction to the states beyond that set out in section 201(b) is misplaced. The issue in *Shreveport* was the Interstate Commerce Commission's authority to set rates for *intra*state rail shipments, *see Houston, E. & W. Texas Ry. Co. v. United States*, 234 U.S. 342 (1914); FERC has not sought to do anything comparable to this. Nothing in the 1935 congressional discussion of *Shreveport* suggests that

B. The Orders Under Review Expressly Provide for Continued State Regulation of Facilities Used in Local Distribution.

Section 201(b) of the FPA leaves to the states jurisdiction over all "facilities used in local distribution." 16 U.S.C. § 824(b). These local distribution facilities are composed of distribution lines connecting retail customers with distribution hubs, at which the high voltage energy transmitted through the grid is converted into lower-voltage energy suitable for distribution and bulk electric energy is subdivided for distribution to retail customers. *See CL&P*, 324 U.S. at 533. Distribution facilities are quite distinct from the high-voltage transmission facilities that make up the interstate grids. *See id.*

Order No. 888 sets forth a seven-factor test for distinguishing between interstate transmission facilities and local distribution facilities, with the express purpose of observing the FPA's jurisdictional division. *See* Order No. 888 at 31,770-71, Pet. App. 281a-283a. California asserts (Cal. Br. at 7-18) that there is no physical distinction between "transmission" and "local distribution" and that an interstate transmission for a retail sale is a part of local distribution. But as Enron showed at pp. 28-31, *supra*, that assertion is wrong. *See* 16 U.S.C. § 824(b) (distinguishing between facilities used for "transmission" and facilities used in "local distribution"); *East Ohio Gas*, 338 U.S. 464 (rejecting argument that, when used to move energy for retail sale, local distribution facilities include interstate transmission facilities). There have been disputes from time to time about whether particular facilities belonged on the "transmission" or the "local distribution" side of the line, but there is no support for California's creative argument that there is no

---

a state, seeking to regulate the total delivered price of goods to its customers, would be free to dictate charges for interstate shipments or to ignore interstate rates set forth in a tariff filed with the ICC.

line at all. There is a line, and it preserves plenary state jurisdiction over facilities used in local distribution.

III. ONLY FERC CAN PROVIDE FOR NONDISCRIMINATORY OPEN ACCESS TO THE INTERSTATE GRIDS.

The practical case for FERC Orders No. 888 and 888-A (and, indeed, for much more complete FERC regulation to secure open access, *see* Enron's brief as petitioner in No. 00-809) may be summarized as follows: (1) Traditional provision of electric service on a monopoly basis by vertically integrated utilities is being supplemented, as a result of congressional action and other factors, by a regime of competition among suppliers of electricity. (2) The new suppliers, including traditional utilities competing outside their native markets, are dependent on nondiscriminatory access to interstate transmission facilities. (3) Nondiscriminatory access can be assured only by requiring the owners and operators of interstate transmission facilities to (a) take transmission on the same terms and conditions as they offer to others, which in turn requires them to (b) publish (and take service pursuant to) open access tariffs covering the reservation of transmission capacity, scheduling of transmission service, the resolution of conflicting demands, the steps to be taken when system constraints require curtailment of transmissions, the charges for transmission, and other similar matters. (4) Because the facilities are connected into interstate grids, only FERC is in a position to impose a workable open access tariff requirement; attempts by the states to mandate nondiscriminatory open access—even if they were motivated to do so—would produce chaos.

FERC's action was needed to safeguard and promote the nationwide competition in the supply of electricity that Congress sought to foster through PURPA and the EPAct, since alternative suppliers cannot compete if they cannot

move their electricity into the markets where it is needed. This objective is even more important today than when Congress enacted these statutes. Several parts of the nation are currently facing electricity shortages made worse by the fact that capacity on the interstate grids is not always available to bring electricity from other parts of the country. *See* Rebecca Smith & John R. Emshwiller, *Down to the Wire: Why California Isn't the Only Place Bracing for Electrical Shock*, Wall St. J., Apr. 26, 2001, at A1; William Claiborne, *Energy Forecasts for Summer: No Blackouts But Price Spikes*, Wash. Post, Apr. 30, 2001, at A3.

The regulation needed to provide nondiscriminatory open access, which is provided in part in Orders No. 888 and 888-A, is not concerned exclusively or even primarily with dollar charges for transmission. It must deal with issues of equal, open, and transparent access to information about the physical state of the transmission grids, uniform procedures for reserving and scheduling transmission capacity, the provision and purchase of various ancillary services that may or may not be provided with transmission, and issues of response to system constraints. Such regulation depends on known rules, contained in a published tariff, that treat comparable suppliers or users comparably. *Cf. AT&T Co. v. Central Office Tel., Inc.*, 524 U.S. 214, 221-22 (1998) (explaining that under the Communications Act every carrier must file a tariff showing all charges, classifications, practices, etc., for the purpose of preventing "unreasonable and discriminatory charges"). Without such published rules, suppliers and users that are dependent on the transmission facilities of others cannot plan, or compete, or offer the same degree of reliability as the transmission owners can promise, and no regulator can police transmission service against undue discrimination.

Only FERC is in a position to require the transmission-owning utilities to file and abide by the needed open access tariff. No state has ever attempted to exercise any such

power; there is no history of state regulation of the terms of access and use of interstate transmission facilities in order to assure appropriate and fair sharing by all competing users. And there are at least three reasons to believe the states could not do so.

First, any attempt by the states to provide detailed terms for access to the interstate grids would raise formidable issues under the dormant Commerce Clause. "[T]ransmission of energy is an activity particularly likely to affect more than one State, and its effect on interstate commerce is often significant enough that uncontrolled regulation by the States can patently interfere with broader national interests." *Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 351, 377 (1983). *Cf. Pennsylvania v. West Virginia*, 262 U.S. 553, 596-97 ("A state law . . . which by its necessary operation prevents, obstructs or burdens such transmission is a regulation of interstate commerce—a prohibited interference."), *aff'd*, 263 U.S. 350 (1923). The Court has stated more than once that the FPA did not grant the states any regulatory powers that the Clause would otherwise have denied. *See Wyoming v. Oklahoma*, 502 U.S. 437, 458 (1992); *New England Power Co. v. New Hampshire*, 455 U.S. 331, 341 (1982) ("Nothing in the legislative history or language of the [FPA] evinces a congressional intent to alter the limits of state power otherwise imposed by the Commerce Clause") (internal quotations and citation omitted).

Second, state regulation of access to the interstate grids would almost inevitably tend to favor in-state uses. Amicus California acknowledges this outright. Its stated purpose for opposing FERC's orders is to obtain the power to allow California utilities to discriminate, in the use of the interstate grid, in favor of California's retail customers: "In times when transmission is short, because of equipment failure or capacity constraints, States commonly require electric utilities to protect first the retail customers to whom public

utility obligations are owed (and in whose interests the utility is given its service monopoly by State law)." (Cal. Br. at 29.)[24] Such a priority for California's retail customers (as compared, for example, with retail customers in another state who are also dependent on transmissions over facilities located in California) may or may not be the best outcome under given conditions, but the state itself is not in a good position to be the judge.[25]

The threat of such parochial state regulation at odds with broader national or regional interests is very real. A similar argument supporting discrimination in favor of in-state customers was upheld by the Eighth Circuit in *Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999), *cert. denied sub nom. Enron Power Mktg., Inc. v. Northern States Power Co.*, 528 U.S. 1182 (2000). There, the court considered the application of Order 888 to certain utilities' systematic preference for their own transmissions over those of their competitors when conditions of system constraint require curtailment of transmissions. *See* Order No. 888 at 31,748-50, 31,923-25, Pet. App. 274a-279a, 325a-330a. The court sustained their power to discriminate. 176 F.3d at 1093.[26]

---

[24] Similarly, Texas has refused to connect to the interstate grids precisely to keep "its" substantial excess capacity to itself, preventing the surplus from being used to provide power to other parts of the country experiencing severe shortages. *See* Alexei Barrionuevo & Russell Gold, *Texas May Face a Glut of Electricity, But That Won't Aid Rest of U.S.*, Wall St. J., May 7, 2001, at A1.

[25] The Court has recognized this in considering the problem of curtailment in the context of transportation of natural gas: "The unavoidable conflict between producing States and consuming States will create contradictory regulations that cannot possibly be equitably resolved by the Courts." *LP&L*, 406 U.S. at 633-64.

[26] FERC opposed Enron's petition for a writ of certiorari in that case, No. 99-916, in part on the ground that the matter should await the D.C. Circuit's decision in the present case, and the petition was denied. 528 U.S. 1182 (2000).

Third, and most fundamental, regulation by all of the states that are connected to each interstate grid simply cannot be expected, in the aggregate, to provide workable rules for access to and usage of the grid. As explained above, the physical flow of power occupies the whole grid because every connected user draws physically on every connected supplier. If there are to be rules governing access to and usage of the grid by competing suppliers and competing users, the rules must as a practical matter be the same or compatible for the entire grid. State-by-state regulation is unworkable. *Cf. Healy v. The Beer Inst.*, 491 U.S. 324, 336 (1989) (burden on interstate commerce depends on "how the . . . [state] statute may interact with the legitimate regulatory regimes of other States and what effect would arise if not one, but many or every, State adopted similar legislation"). State regulation could lead to a balkanization of the grids that could impair effectiveness and reliability and thwart both competition and service to users.

In sum, the problem of access to and usage of the grid by the competing power suppliers that have proliferated in the past two decades is beyond the power of the states to police. The FPA, however, clearly provides FERC with the jurisdiction necessary to prevent this undue discrimination in interstate transmission.[27] New York's argument to the contrary would mean that no regulator at all has jurisdiction to address these critical problems.[28]

---

[27] FERC's historical jurisdiction over interstate transportation of natural gas played a similarly increased role when new forms of competition led FERC to order open access to natural gas pipelines. *See Associated Gas Distribs. v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied sub nom., Interstate Natural Gas Ass'n of America v. FERC*, 485 U.S. 1006 (1988)).

[28] This Court said in *LP&L*, "[W]hen [the Court is] presented with an attempt by the federal authorities to control a problem that is not, by its very nature, one with which state regulatory commissions can be expected to deal, the conclusion is irresistible that Congress desired regulation by federal authority rather than nonregulation." *LP&L*, 406

Finally, there is no reason to accept New York's argument (NY Br. at 46-48) that FERC regulation of interstate transmission for retail sales will adversely affect maintenance, customer service, and reliability of the grids, and that FERC will set inadequate rates for transmission, creating inadequate incentives for construction of new transmission lines. Contrary to New York's assertions, there is every reason to believe that it is federal, not state, regulation that is needed to improve the grids and make them fully adequate to meet present and future demand. *See* John J. Fialka & Bob Davis, *Cheney Panel Considers Helping Utilities Expand Hydro Power Transmission Lines*, Wall St. J., May 3, 2001, at A2:

> The task force on energy strategy, led by Vice President Dick Cheney . . . is expected to urge [FERC] to boost the rates that utilities can charge customers for transmitting electricity. The higher rates would encourage the construction of new power lines.
>
> * * * *
>
> In the case of electricity transmission, the White House has been looking for ways to unclog the nation's power grid without having the federal

U.S. at 641 (quoting *FPC v. Transcon. Gas Pipe Line Corp.*, 365 U.S. 1, 28 (1961)) (internal quotations omitted); *see also id.* at 631 ("[I]n a borderline case where congressional authority is not explicit [, the Court] must ask whether state authority can practicably regulate a given area and, if . . . it cannot, then [the Court is] impelled to decide that federal authority governs.") (internal quotations and citation omitted). In 1935, the Senate Report explained that the purpose of the FPA was to fill not only the "Attleboro gap," but also "[o]ther features of this interstate utility business that are equally immune from State control either legally or practically." S. Rep. No. 74-621, at 17. This Court noted that "Congress' purpose in 1935 was to fill a regulatory gap, not to perpetuate one." *Arkansas Elec.*, 461 U.S. at 384. There is no reason not to interpret the FPA to allow FERC to fill an important gap.

> government string new power lines and build new stations as it once built the interstate highway system.
>
> The White House wants to encourage utilities to speed construction by increasing the regulated return on their investment in new transmission facilities . . . .[29]

At the very least, federal regulators have as strong an incentive as any state regulator to focus on long-range solutions to the problem of energy transmission, rather than on protecting particular groups of users.

[29] In fact, on March 14, 2001, FERC issued an order proposing several initiatives "to protect consumers from supply disruptions . . . [i]n light of the severe electric energy shortages facing California and other areas of the West in recent months." The order also invited comments on, among other things, (1) premiums on equity returns and accelerated depreciation periods for projects that increase transmission capacity, and (2) recovery of a return on non-capital intensive expenditures made to increase transmission capacity on constrained interfaces (e.g., technologies that improve voltage control and power flows). *See Removing Obstacles to Increased Electric Generation and Natural Gas Supply in the Western United States*, 94 F.E.R.C. ¶ 61,272, at 61,967 (2001).

CONCLUSION

The decision of the court of appeals sustaining FERC's orders should be affirmed as to the claims asserted in New York's petition.

Respectfully submitted,

JEFFREY D. WATKISS
BRACEWELL & PATTERSON, L.L.P.
2000 K Street, N.W.
Suite 500
Washington, D.C. 20006
(202) 828-5800

JOSEPH R. HARTSOE
SARAH NOVOSEL
ENRON CORP.
1775 I Street, N.W.
Washington, D.C. 20006
(202) 828-3360

LOUIS R. COHEN
Counsel of Record
JOSEPH E. KILLORY, JR.
JONATHAN J. FRANKEL
IJAY PALANSKY
MICHAEL PLOTNICK
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000

Counsel for Respondent Enron Power Marketing, Inc.

May 10, 2001

MAY 31 2001

Nos. 00-568 & 00-809

Supreme Court, U.S.
FILED
MAY 31 2001
CLERK

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

---

BRIEF OF RESPONDENT EDISON ELECTRIC INSTITUTE

EDWARD H. COMER
BARBARA A. HINDIN
EDISON ELECTRIC INSTITUTE
701 Pennsylvania Ave., N.W.
Washington, D.C. 20004
(202) 508-5000

CHARLES G. COLE
Counsel of Record
DAVID B. RASKIN
ALICE E. LOUGHRAN
STEPTOE & JOHNSON LLP
1330 Connecticut Ave., N.W.
Washington, D.C. 20036
(202) 429-6270

Counsel for Respondent Edison Electric Institute

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

BEST AVAILABLE COPY

QUESTIONS PRESENTED

Section 201(b) of the Federal Power Act ("FPA") grants the Federal Regulatory Energy Commission ("FERC") jurisdiction over "the transmission of electric energy in interstate commerce" and "the sale of electric energy at wholesale in interstate commerce" but not over "any other sale of electric energy." The questions presented are:

1. Whether FERC correctly concluded that it has jurisdiction under FPA § 201(b) over interstate transmission service that has been unbundled and sold separately from the sale of electric energy to a retail customer?

2. Whether FERC correctly concluded that it lacks jurisdiction under FPA § 201(b) over interstate transmission provided as part of a sale of electric energy in a single, bundled transaction with a retail customer?

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
OPINIONS BELOW	1
JURISDICTION	1
STATUTORY AND REGULATORY PROVISIONS INVOLVED	1
STATEMENT OF THE CASE	1
I. BACKGROUND	3
A. Edison Electric Institute	3
B. Changes in the Retail Electric Industry	3
C. Changing Uses on The Interstate Grid	4
II. RESTRUCTURING OF THE ELECTRIC INDUSTRY	7
A. Order No. 888	7
B. Decision of the Court of Appeals	9
C. State Unbundling Following Order No. 888	10
SUMMARY OF THE ARGUMENT	11
ARGUMENT	15
I. FERC LAWFULLY ASSUMED JURISDICTION OVER UNBUNDLED INTERSTATE TRANSMISSION SERVICE PROVIDED TO RETAIL CUSTOMERS.	15
A. The Rule Properly Applies to Transmission in Interstate Commerce	16
B. Transmission Unbundled From a Retail Sale Does Not Fall Within Any of the Exceptions to Section 201(b).	21

TABLE OF CONTENTS—Continued

	Page
C. The Legislative History Does Not Contradict The Plain Language Used In the Statute	26
D. New York Cannot Defeat the Language of the Statute By Reliance On Presumptions Regarding Preemption	30
E. All Retail Transmission Does Not Fall Under The Exception for Local Distribution	32
II. FERC LAWFULLY DECLINED TO ASSERT JURISDICTION OVER TRANSMISSION THAT IS BUNDLED WITH A RETAIL SALE	36
A. Enron Ignores Statutory Language That Preserves Pre-Existing State Jurisdiction Over Bundled Retail Sales.	37
B. The NGA Case Law Does Not Compel a Conclusion That FERC Has Jurisdiction Over Bundled Retail Transmission.	41
C. Regulation of Bundled Sales Is Not Necessary to Fulfill the Stated Objectives of Order No. 888.	45
CONCLUSION	50
APPENDIX	
Sections 201(a)-(d) of the FPA, 16 U.S.C. §§ 824(a)-(d)	1a
Section 212(h) of the FPA, 16 U.S.C. § 824k(h)	3a
Section 313(b) of the FPA, 16 U.S.C. § 825*l*(b)	4a
Sections 1(a) and (b) of the NGA, 15 U.S.C. §§ 717(a), (b)	5a
Section 7(c) of the NGA, 15 U.S.C. § 717f(c)	6a
18 C.F.R. § 35.28	7a

TABLE OF AUTHORITIES

CASES:

	Page
Algonquin Gas Transmission Co. v. FERC, 809 F.2d 136 (1st Cir. 1987)	44
Appalachian Power Co. v. Public Service Commission of West Virginia, 812 F.2d 898 (4th Cir. 1987)	29
Arkansas Electric Cooperative Corp. v. Arkansas Public Service Comm'n, 461 U.S. 375 (1983)	20, 26, 29
Arkansas Louisiana Gas Co v. Hall, 453 U.S. 571 (1981)	42
Bob Jones University v. United States, 461 U.S. 574 (1983)	40
CFTC v. Schor, 478 U.S. 833 (1986)	41
Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984)	45
Cipollone v. Liggett Group, Inc., 505 U.S. 504 (1992)	30
Cities of Aitkin v. FERC, 704 F.2d 1254 (D.C. Cir. 1982)	43
Cities of Newark v. FERC, 763 F.2d 533 (3d Cir. 1985)	47
City of Orville v. FERC, 147 F.3d 979 (D.C. Cir. 1998)	19
Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945)	*passim*
Davis v. Michigan Department of the Treasury, 489 U.S. 803 (1989)	26
East Ohio Gas Co. v. Tax Commission of Ohio, 283 U.S. 465 (1931)	33, 34
FDA v. Brown & Williamson Tobacco Corp., 529 U.S. 120 (2000)	40
FERC v. Mississippi, 456 U.S. 742 (1982)	20

TABLE OF AUTHORITIES—Continued

	Page
FPC v. Colorado Interstate Gas Co., 348 U.S. 492 (1955)	19
FPC v. East Ohio Gas Co., 338 U.S. 464 (1950)	24, 35, 44
FPC v. Florida Power & Light Co., 404 U.S. 453 (1972)	*passim*
FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972)	41, 44, 45
FPC v. Southern Cal. Edison Co., 376 U.S. 205 (1964)	23, 26, 35
Florida Power & Light Co. v. EPA, 145 F.3d 1414 (D.C. Cir. 1998)	18
Fort Pierce Utilities Authority v. FERC, 730 F.2d 778 (D.C. Cir. 1984)	5
Gainesville Utilities Department v. Florida Power Corp., 402 U.S. 515 (1971)	5
General Motors Corp. v. Tracy, 519 U.S. 278 (1997)	22, 47, 48
Gorbach v. Reno, 219 F.3d 1087 (9th Cir. 2000)	23
Gulf States Utilities Co. v. FERC, 1 F.3d 288 (5th Cir. 1993)	19
Gulf States Utilities Co. v. FPC, 411 U.S. 747 (1973)	29
Jones v. Rath Packing Co., 430 U.S. 519 (1977)	30
Kennecott Utah Copper Corp. v. U.S. Department of Interior, 88 F.3d 1191 (D.C. Cir. 1996)	18
Knickerbocker Ice Co. v. Stewart, 253 U.S. 149 (1920)	23
Louisiana Public Service Commission v. FCC, 476 U.S. 355 (1986)	31
Metropolitan Edison Co. v. FERC, 595 F.2d 851 (D.C. Cir. 1979)	47

TABLE OF AUTHORITIES—Continued

	Page
Mississippi Power & Light Co. v. Mississippi, 487 U.S. 354 (1988)	30
NLRB v. Bell Aerospace Co., 416 U.S. 267 (1974)	40
New England Power Co. v. New Hampshire, 455 U.S. 331 (1982)	20
Northeast Utilities Service Co. v. FERC, 993 F.2d 937 (1st Cir. 1993)	47, 48
Northern States Power Co. v. FERC, 176 F.3d 1090 (8th Cir. 1999), *cert. denied*, 528 U.S. 1182 (2000)	47
Panhandle Eastern Pipe Line Co., 232 F.2d 467 (3d Cir.), *cert. denied*, 352 U.S. 891 (1956)	44
Pennsylvania Gas Co. v. Public Service Commission, 252 U.S. 23 (1920)	25, 28, 38
Pennsylvania v. West Virginia, 262 U.S. 553 (1923)	42
Phillips Petroleum Co. v. State of Wisconsin, 347 U.S. 672 (1954)	24
Public Service Co. of Ind., Inc. v. FERC, 575 F.2d 1204 (7th Cir. 1978)	47
Public Utilities Commission of Rhode Island v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927)	24, 25, 28
Rice v. Santa Fe Elevator Corp., 331 U.S. 218 (1947)	30
Russello v. United States, 464 U.S. 16 (1983)	26
Smiley v. Citibank (South Dakota), N.A., 517 U.S. 735 (1996)	30
South Carolina Power Co. v. South Carolina Tax Commission, 52 F.2d 515 (E.D.S.C. 1931), *aff'd*, 286 U.S. 525 (1932)	34

TABLE OF AUTHORITIES—Continued

	Page
South Covington & Cincinnati St. Railway v. City of Covington, 235 U.S. 537 (1915)	25
St. Michaels Utilities Commission v. FPC, 377 F.2d 912 (4th Cir. 1967)	47
United Parcel Service, Inc. v. Mitchell, 451 U.S. 56 (1981)	33
United States v. Cleveland Indians Baseball Co., 121 S. Ct. 1433 (2001)	40
United States v. Oregon, 366 U.S. 643 (1961)	26
United States v. Public Utilities Commission of Cal., 345 U.S. 295 (1953)	35
Wabash St. L & P. Railway v. State of Illinois, 118 U.S. 557 (1886)	25
STATE CASES	
Mill Creek Coal & Coke Co. v. Public Service Commission, 100 S.E. 557 (W. Va. 1919)	24, 25, 28, 38
People ex. rel Horton v. Prendergast, 162 N.E. 10 (N.Y. 1928)	40
FEDERAL STATUTES	
Federal Power Act	
Section 201(a) of the Federal Power Act, 16 U.S.C. § 824(a)	*passim*
Section 201(b) of the Federal Power Act, 16 U.S.C. § 824(b)	*passim*
Section 201(c) of the Federal Power Act, 16 U.S.C. § 824(c)	*passim*
Section 212(h) of the Federal Power Act, 16 U.S.C. § 824k(h)	*passim*
Section 313(b) of the Federal Power Act, 16 U.S.C. § 825*l*(b)	1, 18, 32

TABLE OF AUTHORITIES—Continued

	Page
Natural Gas Act	
Sections 1(a) of the Natural Gas Act, 15 U.S.C. § 717(a)	1
Section 1(b) of the Natural Gas Act, 15 U.S.C. § 717(b)	1, 43
Section 7(c) of the Natural Gas Act, 15 U.S.C. § 717f(c)	1, 15, 43, 44
Section 19(b) of the Natural Gas Act, 15 U.S.C. § 717r(b)	19
Other Federal Statutes	
28 U.S.C. § 1254(1) (1994)	1
Energy Policy Act, Pub. L. No. 102-486, 106 Stat. 2776 (1992) (EPAct)	7, 40
Public Utilities Regulatory Policy Act, Pub. L. No. 95-617, 92 Stat. 3117 (1978) ("PURPA")	7, 40
STATE STATUTES	
Conn. Gen. Stat. § 16-244b	22
Conn. Gen. Stat. § 16-244e	22
Me. Rev. Stat. Ann. Tit. 35-A § 3202	22
Del. Code Ann. Tit. 26 § 1003	22
Okla. Stat. Ann. Tit. 17 § 190.4	22
Okla. Stat. Ann. Tit. 17 § 190.2	11
LEGISLATIVE MATERIALS	
H.R. Rep. No. 74-1318 (1935)	39
S. Rep. No. 74-621 (1935)	28, 39
79 Cong. Rec. 10,352, 10,377 (June 28, 1935)	28
Hearings on H.R. 11662 Before House Committee on Interstate and Foreign Commerce, 74th Cong. 117 (1936)	42

TABLE OF AUTHORITIES—Continued

Page

Hearings on H.R. 11662 Before House Committee on Interstate and Foreign Commerce, 74th Cong. 56 (1936) 43
Pub. Util. Holding Cos.: Hearings on H.R. 5423 Before the House Committee on Interstate and Foreign Commerce, 74th Cong. 521-22 (1935) 39
Public Utility Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce, 74th Cong. 797 (1935) (Memorandum of Oswald Ryan, FPC General Counsel, and Dozier A. DeVane, FPC Solicitor) 29

ADMINISTRATIVE REGULATIONS & NOTICES

18 C.F.R. § 35.28 (2000) 1, 16
Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking, 59 Fed. Reg. 35,274, 35,284 (July 11, 1994) 17
Promoting Wholesale Competition Through Open-Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, 60 Fed. Reg. 17,662 (Apr. 7, 1995) ("Open Access NOPR") 27

ADMINISTRATIVE CASES

Arizona Public Service Co. v. Idaho Power Co., 87 F.E.R.C. (CCH) ¶ 61,303(1999) 48

TABLE OF AUTHORITIES—Continued

Page

Capacity Benefit Margin in Computing Available Transmission Capacity, Order Clarifying Methodology for Computing Available Transmission Capability, 88 F.E.R.C. (CCH) ¶ 61,099 (1999) 48
El Paso Electric Co., 87 F.E.R.C. (CCH) ¶ 61,202 (1999) 48
Northeast Utilities Service Co., 59 F.E.R.C. (CCH) ¶ 61,042 (1992), *aff'd*, 993 F.2d 937 (1st Cir. 1993) 47
Wisconsin Power & Light Co., 84 F.E.R.C. (CCH) ¶ 61,120 (1998) 48

TREATISES & ARTICLES

BONBRIGHT, JAMES C., ET AL., PRINCIPLES OF PUBLIC UTILITY RATES (1988) 43
Brown, Hon. Ashley C., *State Power Over Transmission Access and Pricing: The Giant Will Not Sleep Forever*, 124 Pub. Utils. Fort. (1989) 40
KAHN, EDWARD, ELECTRIC UTILITY PLANNING AND REGULATION (1988) 43

OPINIONS BELOW

The opinion of the court of appeals is reported at 225 F.3d 667. Pet. App. 3a-121a.[1] The pertinent orders of the Federal Energy Regulatory Commission ("FERC"), Order No. 888 and Order No. 888-A, are reported at 61 Fed. Reg. 21,540 and 62 Fed. Reg. 12,274, respectively. Relevant portions also appear at Pet. App. 125a-369a and 371a-551a.

JURISDICTION

The judgment of the court of appeals was entered on June 30, 2000, and the petitions for rehearing were denied on August 22, 2000. Pet. App. 3a, 123a-124a.

The petitions for a writ of certiorari were filed on October 12, 2000 and November 20, 2000, and were granted on February 26, 2001. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) (1994).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Sections 201(a)-(d), 212(h), and 313(b) of the Federal Power Act of 1935 ("FPA"), 16 U.S.C. §§ 824(a)-(d), 824k(h), 825*l*(b) (1994); and Sections 1(a), (b), and 7(c) of the Natural Gas Act ("NGA"), 15 U.S.C. §§ 717(a), (b), 717f(c) (1994); and 18 C.F.R. § 35.28 (2000) (the open access regulation) are reproduced in relevant part in an appendix to this brief. App., *infra*, 1a-8a.

STATEMENT OF THE CASE

The Nation's electric industry is in transition. Over the past decade, FERC has opened the market for wholesale electric power sales to competition. In addition, in many states, the traditional industry model of a single vertically-integrated firm providing retail service to a customer has

---

[1] "Pet. App." refers to the appendix to the petition for a writ of certiorari filed by Enron Power Marketing, Inc. ("Enron") in No. 00-809.

given way to competition for the supply of electric energy to retail customers. In order to permit such competition, states have ordered or permitted utilities to "unbundle" their transmission services—to sell retail transmission service independently of electric energy. FERC's issuance of Order No. 888 was a keystone event in this transition, prescribing uniform rules of access to transmission in wholesale energy markets and in those retail markets in which the states have permitted competition for electric energy.

Respondent Edison Electric Institute ("EEI") submits this brief in support of FERC's decision on the jurisdictional issues in Order No. 888. FERC concluded that it possessed exclusive jurisdiction over interstate transmission service that has been unbundled from a retail sale of energy, but lacked jurisdiction over transmission that was a component of a bundled retail sale. This interpretation has been challenged both for overreaching and for failing to assert jurisdiction granted by Congress.

EEI urges this Court to reject both attacks. Order No. 888 represents a sound construction of the language of the Federal Power Act. Retail transmission sold separately from energy falls within the statutory grant of jurisdiction for "the transmission of electric energy in interstate commerce," while a transmission sold as part of a sale of energy to retail customers falls within its exception for "any other sale of electric energy." 16 U.S.C. § 824(b)(1). This interpretation protects service to retail customers in states that follow the traditional model, while ensuring that competing energy suppliers receive equal access to transmission facilities in states that have opened retail markets to competition. It is well suited to a nation in which different states are following different courses with respect to retail competition.

I. BACKGROUND

A. Edison Electric Institute

EEI is the national association of U.S. shareholder-owned electric companies, their affiliates and industry associates worldwide. Its members are located in forty-nine States and the District of Columbia. EEI's members serve over ninety percent of all customers served by the shareholder-owned segment of the industry. They generate approximately three quarters of all the electricity generated by electric companies and serve about seventy percent of all retail customers in the nation. EEI members own approximately seventy percent of all transmission facilities in the country.

EEI members participate in all aspects of the restructured electric industry. EEI members include companies that provide traditional bundled service under an obligation to serve retail customers and companies operating in states that have adopted retail competition. Some EEI members are vertically integrated, some have separated their generation, transmission and distribution into separate business units or affiliates, and others have divested portions of their electric businesses. All EEI members are public utilities subject to FERC jurisdiction, and they provide open access transmission service over their transmission facilities as required by Order No. 888. Many EEI members participated in the proceedings below and were named as respondents in the petitions for certiorari.

B. Changes in the Retail Electric Industry

When Congress enacted the Federal Power Act in 1935, there was no such thing as unbundled retail transmission service. In 1935 and for many decades thereafter, the vast majority of electric service to consumers was provided by vertically-integrated utility companies subject to state regulation. Pet. App. 28a, 141a. Their service combined generation with delivery of electric power into a single bundled service. Pet. App. 9a, 27a, 141a. The retail

customer had no choice among providers, and the rates, terms and conditions of the delivered service were fully regulated by the States. Pet. App. 28a, 30a. As of this time, many states have retained the traditional model of the franchised utility as the preferred means of providing quality service to their retail customers.

In the past decade, however, a number of states have decided to open their retail markets to competition among energy suppliers. Pet. App. 132a. As a critical first step, they have directed or permitted the utilities in their jurisdiction to provide transmission service independently of energy. This enables other potential suppliers of energy to purchase the transmission service for use in selling their own energy to retail customers. This unbundling of transmission service represents a paradigm shift from the franchised, vertically-integrated utility to a competitive marketplace in which different firms seek to provide different aspects of electric service directly to retail customers. And it has transformed the primary role of regulation from supervising the rates, terms and conditions of bundled service to assuring that competition among energy suppliers for the same retail customers takes place under fair conditions.

C. Changing Uses on The Interstate Grid

The role of the interstate grid has also changed dramatically in recent years. Traditionally, utilities built transmission lines for the benefit of their own customers and with funds supplied by those customers. Pet. App. 28a, 141a. Their principal purpose was to transmit power from nearby sources of generation and within their retail service areas. *Id.* Gradually, utilities began interconnecting their systems permitting the exchange of electric energy in a wholesale market, but until relatively recently these exchanges usually involved transactions between the utilities themselves.

Since the enactment of the Federal Power Act, electric utilities have constructed thousands of miles of high voltage transmission lines linking ("interconnecting") their systems across state lines. Pet. App. 10a, 147a. These interconnections were created to coordinate operations and thereby enhance the reliability of the utilities' systems, as well as to engage in sales of electric energy with each other. *See Gainesville Utils. Dep't v. Florida Power Corp.*, 402 U.S. 515, 520-24 (1971); Pet. App. 10a, 141a, 147a. They were also constructed to enable utilities to participate jointly in large generating projects located at a distance from the utilities' service territories. Pet. App. 147a. Over the past three decades or so, this construction has produced highly integrated regional transmission networks over which electric power flows freely between systems and across state lines. *Id.*

Although the interstate transmission grid consists primarily of transmission lines planned and built by individual utilities, in many respects the grid functions like a reservoir full of water: "a given amount of power enters the system at one point and a like amount is delivered at another point." *Fort Pierce Utils. Auth. v. FERC*, 730 F.2d 778, 782 (D.C. Cir. 1984). The original producer of electrons has no control over them after they enter the transmission grid because they commingle with other electrons from different sources. Even though each increment of production by a given generator expands the supply of energy available to meet demand on the electric system, the electrons added to the interstate grid by a particular generator will not necessarily be those that reach his buyer.

As one petitioner aptly put it in the proceedings below: "electrons do not respect State boundaries."[2] Electrons

---

[2] Request of the National Association of Regulatory Utility Commissioners for Rehearing of Order No. 888, at 9 (May 4, 1996) (FERC Docket Nos. RM95-8-00 and RM94-7-001).

follow the laws of physics, rather than contract rights or regulatory law. On the interconnected AC network, electrons disperse onto the various available transmission lines, and electrons seek the path of least electrical resistance under Ohm's law. The configuration of regional generation use, available transmission lines and the location of electrical loads all affect the pattern of flows on the interconnected grid. Thus, such patterns of flow are complicated, dynamic and not necessarily congruent with the contractual path of an identified transaction.[3] Through these multiple, indirect paths, the grid moves energy in bulk quantities over significant distances and from one local area to another.

The "local distribution facilities" of electric utilities are different. These facilities operate at lower voltages and do not transfer large quantities of electricity for long distances across broad geographic regions. Pet. App. 350a-351a, 368a. Rather, utilities own and operate "substations" at which power is received from high voltage transmission lines, voltages are reduced ("stepped down"), and power is then sent into the lower capacity distribution lines for delivery to end-use consumers. Pet. App. 350a-351a, 360a. Distribution facilities typically operate like appendages to the transmission system, with power flowing radially out from the transmission grid to ultimate consumers. As defined by the Commission, local distribution facilities are typically those into which power may enter but from which it does not exit.

---

[3] *See* Comments of North Carolina Utilities Commission at 4 n.2 ("[T]he actual path taken by electric power flow across a transmission system is difficult to predict. Because of its interconnection with neighboring systems, a transmission system typically consists of a number of possible paths between any two points. . . [T]he actual flow of electricity typically diverges significantly from the contract path, with the result that the supposed economics of the contract path frequently have little to do with the actual cost of the power transfer.") (Aug. 10, 1995) (Order No. 888 Rulemaking Proceedings, FERC Docket Nos. RM95-8-00 and RM94-7-001).

Pet. App. 36a n.6. Thus, power flows in a distribution facility rarely have a material impact on transmissions of electricity in bulk quantities on the interstate grid.

II. RESTRUCTURING OF THE ELECTRIC INDUSTRY

By the 1970s, some electric industry participants began looking at interstate transmission as a means of enabling them to compete in the supply of electric power at the wholesale level. Pet. App. 10a, 29a. In 1978, as a response to the energy crises of the 1970s, Congress enacted the Public Utilities Regulatory Policy Act, Pub. L. No. 95-617, 92 Stat. 3117 (1978) ("PURPA"). PURPA spawned the development of a new, non-utility generation industry that began demanding access to the interstate transmission grid in order to compete with utility-owned generation.

In 1992, Congress enacted the Energy Policy Act, Pub. L. No. 102-486, 106 Stat. 2776 (1992) (EPAct), which expanded FERC's authority to order utilities to provide interstate transmission service as a separate unbundled product. However, Congress expressly limited this authority to ordering "wholesale" transmission services, thereby preserving to the States the authority to continue regulating bundled retail services, and to choose whether and under what terms competition for retail sales of electric energy might be permitted. To this end, Congress expressly prohibited FERC from ordering wheeling directly to an end-user and prohibited sham transactions designed to circumvent the ban on mandatory retail wheeling. 16 U.S.C. § 824k(h).

A. Order No. 888

By 1995, the competitive market for wholesale power had evolved to the point that FERC perceived a risk that transmission-owning utilities could favor their own merchant activities (*i.e.*, wholesale power transactions) by offering transmission services to competitors on discriminatory

terms. Pet. App. 557a-559a, 566a. In Order No. 888, FERC ordered every transmission-owning public utility subject to its jurisdiction to file an open access transmission tariff with uniform terms and conditions of service under which it would supply transmission both for its own wholesale transactions and for those of its competitors. Pet. App. 133a-134a.

Further, FERC determined that where interstate transmission was provided to retail customers separately from a sale of energy, it would also be subject to the open access tariff, thereby ensuring that such services would be provided on a non-discriminatory basis to competing energy providers. Pet. App. 136a, 305a. However, the Commission did not apply its open access transmission requirements to state-regulated, bundled retail electric sales, which are not supplied in a competitive market. Pet. App. 306a. Rather, consistent with the Energy Policy Act, it respected the right of individual states to decide whether retail services should be unbundled to permit competition for such services and, absent such competition, allowed the states to continue to regulate all components of bundled retail service. Pet. App. 305a-306a.

Even with respect to unbundled retail transmission services, Order No. 888 specifically preserved state jurisdiction over local distribution facilities used to deliver energy to end-users. Pet. App. 282a-283a, 310a-312a. FERC proposed seven physical characteristics that could be used to distinguish such distribution facilities from electric transmission.[4] As a matter of process, FERC said that public

[4] The seven indicators of local distribution are: (1) close proximity to retail customers; (2) radial design; (3) inflows are common, outflows are rare; (4) power is not reconsigned or transported on to other markets; (5) power is consumed in a comparatively restricted geographical area; (6) meters measure flows at the interface between transmission and local distribution; and (7) distribution systems feature reduced voltage. Pet. App. 282a-283a.

utilities must consult with their state regulatory authorities before petitioning FERC for a ruling on the proposed classification and that FERC would defer to state recommendations on where to draw the line. Pet. App. 312a.[5]

The Commission also addressed in Order No. 888 various issues relating to the rights of different entities to access the grid when transmission capacity is insufficient to handle all of the competing transactions. Pet. App. 264a-274a. It permitted utilities to reserve sufficient transmission capacity on their systems to serve reliably their bundled retail service customers, the so-called "native load." However, it also established requirements concerning the calculation of remaining available transmission capacity ("ATC"), which would be utilized to establish the quantity of capacity available for customers under the open access tariffs. Order No. 888, 61 Fed. Reg. 21,540, 21,574-75 (May 10, 1996); Pet. App. 267a-72a. Further, FERC asserted authority to review such determinations of ATC, including the "set-aside" for bundled retail service (*i.e.*, for "native load"), to ensure that transmission capacity would not be withheld arbitrarily from the open access market. Order No. 888-A, 62 Fed. Reg. 12,274, 12,301 (Mar. 14, 1997); *see also* note 42 *infra*. In addition, once a utility determines that sufficient ATC exists to provide service under the open access regime, the priority rules established in Order No. 888 mandate the same level of "firmness" to open access transmission customers in comparison with bundled retail customers. Pet. App. 269a-270a.

B. Decision of the Court of Appeals

The court of appeals upheld FERC's conclusions with regard to jurisdiction. It agreed with FERC that the definition

[5] Since the promulgation of the final rule in 1996, FERC has not overruled any state commission recommendation with respect to the extent of local distribution.

of interstate transmission in FPA § 201(c), as construed by this Court's decisions, was broad enough to provide jurisdiction over retail as well as wholesale transmission. Pet. App. 35a. Thus, the court of appeals rejected New York's argument that FERC lacked jurisdiction over unbundled retail transmission.

The court also agreed with FERC that FERC was not required to mandate unbundling and assert jurisdiction over all retail transmissions. "Just as FPA Section 201 gives FERC jurisdiction over transmissions in interstate commerce and sales at wholesale, the statute also clearly contemplates state jurisdiction over local distribution facilities and retail sales." Pet. App. 35a. In the court's view, "[a] regulator could reasonably construe transmissions bundled with generation and delivery services and sold to a consumer for a single charge as either transmission services in interstate commerce or as an integral component of a retail sale." *Id.* The Court upheld FERC's decision to characterize a bundled transmission as part of a retail sale as a "statutorily permissible policy choice." *Id.*

Finally, the court rejected New York's argument that the seven-factor test used for identifying local distribution in the context of retail transmissions should also be used for wholesale transmissions. The court held that the FPA gave FERC jurisdiction over all aspects of a wholesale transmission, regardless of the facility involved. Pet. App. 38a-39a.

C. State Unbundling Following Order No. 888

At the time FERC issued Order No. 888, no state had fully unbundled retail service, permitting competition for retail customers. In a few states, there were limited experiments permitting large customers to seek alternative suppliers. Following Order No. 888, a significant number of states enacted legislation or rules mandating the unbundling of retail

services.[6] All of these states were aware of the jurisdictional implications of Order No. 888, and in some cases specifically referred to it in the retail access legislation.[7] Other states have declined to embrace retail competition, or have chosen to defer its implementation.

SUMMARY OF THE ARGUMENT

Order No. 888 respects the division of federal and state authority drawn by Congress in the FPA, while taking into account the changes that have taken place since the Act was enacted. It protects the legitimate interests of retail customers who depend upon a single utility providing traditional retail service, while ensuring fair access to transmission facilities in those markets where the supply of electricity has become the subject of competition, often on an interstate basis. Because Order No. 888 is soundly based in the language of the FPA and consistent with its objectives, it should be affirmed.

Both sets of challengers proceed on the same core assumption that unbundling is merely an artificial accounting convention and, from that premise, reach opposite conclusions. Both are wrong. Unbundling represents a fundamental change in the way that utilities do business, with important legal and economic implications. From a legal perspective, the unbundling of transmission means that transmission is sold in commercial transactions separate from

---

[6] States that have ordered retail competition include: Arizona, Arkansas, California, Connecticut, Delaware, Illinois, Maine, Maryland, Massachusetts, Michigan, Montana, Nevada, New Hampshire, New Jersey, New Mexico, New York, Pennsylvania, Oklahoma, Oregon, Rhode Island, Texas, and Virginia. Current information about the status of various state retail programs, as well as some corresponding citations, may be found at www.eia.doe.gov/cneaf/electricity/chg_str/tab5rev.html.

[7] *See, e.g.*, Okla. Stat. Ann. Tit. 17 § 190.2; *see also* Brief of Amici Curiae State of California at 1 (admitting that California made its choice regarding retail competition knowing FERC's position on the jurisdictional issue).

the sale of electric energy. From an economic perspective, unbundling is a means of introducing competition into an electric market, and thereby creates a need for rules to prevent discrimination against competitors seeking to enter that market. Order No. 888 recognizes the significance of these distinctions, while reasonably characterizing traditional bundled transmission service as integral to a retail sale of energy and hence outside the Commission's jurisdiction.

New York and its allied petitioners ("New York") question whether retail transmission involves interstate commerce. However, the Commission relied on settled law and universally accepted scientific fact when it posited that retail transmission over the interconnected grid would be "in interstate commerce." 16 U.S.C. §§ 824(b), (c). New York failed to challenge that point before the Commission and failed to raise in the court of appeals the largely factual issues that it presents here. This case must therefore be decided on FERC's premise that its rule was directed at interstate transmission.

FERC's rule accords with FPA § 201(b), which grants federal jurisdiction over interstate transmission without a limitation to wholesale transactions. It therefore encompasses transmission service to retail customers when that service is sold separately from energy. Indeed, this intent is confirmed by the wording of the proviso to § 201(b), which excepts only "any other sale of electric energy." A separate sale of unbundled transmission service is not a "sale of electric energy." 16 U.S.C. § 824(b).

New York relies heavily upon FPA § 201(a), but that declaration of policy does not override the express grants of jurisdiction in the statute. Moreover, by its own terms, § 201(a) does not apply here. At most, this section states an intention to preserve for the States their jurisdiction over matters that they were regulating at the time of enactment. These did not, of course, include interstate transmission

divorced from retail sales. Indeed, "direct" state regulation of interstate transmission independent of a retail transaction would likely have been viewed as unconstitutional. Thus, such jurisdiction was not saved, and certainly was not granted, by § 201(a).

New York quotes extensively from the legislative history of the FPA. To the extent that such history is meaningful at all, it confirms that Congress intended to save for the states their "pre-existing jurisdiction," which involved bundled retail sales. It also shows an intent to have federal jurisdiction fill any gap that was created by constitutional limitations on state jurisdiction over interstate transmission—limitations that were already apparent at the time of enactment. Thus, FERC has acted in conformity with congressional intent when it has assumed jurisdiction over transmission facilities used in the new competitive interstate markets created by state restructuring.

Finally, New York cannot rely on a presumption against federal preemption of the States' traditional police powers. The question of whether FERC has authority over unbundled sales of transmission is not a question of preemption but rather of jurisdiction. Questions of agency jurisdiction are determined by its organic statute, without reference to presumptions. This is especially true with respect to the FPA, which contains its own detailed jurisdictional provisions. Thus, this Court has never referred to presumptions in analyzing those provisions.

Amici California and California Public Service Commission ("California") seek reversal on completely different grounds, contending that all retail transmission falls within § 201(b)'s exemption for "local distribution." This argument is not properly before the Court because it was not presented to the Commission, to the court of appeals or to this Court in the petition for certiorari. In fact, petitioner New York actually endorsed the use of the seven-factor test announced

by the Commission as the means of identifying which facilities are involved in "local distribution."

In any event, FERC's interpretation is faithful to the language of this provision and the governing case law. There would be no point in an exemption for "any other sale" if local distribution covered all retail sales. "Local distribution" has a narrower meaning, consistent with pre-enactment case law that identified "local distribution" as occurring when gas pressure or voltage was reduced for purposes of retail delivery. Post-enactment case law has confirmed that the identification of "local distribution" facilities is a question of fact to be decided by the Commission. The Commission's use of a seven-factor test to identify such facilities has not been shown to be arbitrary or capricious. Thus, this exception does not remove all retail transmission from FERC's jurisdiction.

Enron, seeking federal jurisdiction over transmission for bundled retail sales, contends that § 201(b) of the FPA "gives FERC jurisdiction, without any stated limitation or qualification, over all interstate transmissions of electric energy." Brief of Enron in No. 00-809 ("Enron Br.") at 21. This argument, however, ignores both the "any other sale" proviso of § 201(b)—specifically excluding retail sales of power from FERC jurisdiction—and the six decades of history leaving to the States jurisdiction over any transmission sold as part of the retail power sale. Congress has amended the FPA on several occasions, but has not altered this allocation of responsibility.

Enron relies for support almost exclusively on case law under the Natural Gas Act. This case law is not dispositive, since the natural gas industry developed along different lines than the electric industry. From the outset, natural gas was transported by interstate pipelines owned by different companies than were responsible for production and distribution. Congress sought to place this separate interstate

transportation function under federal control by adopting a certification requirement in § 7(c) of the NGA, which has no counterpart in the FPA. In order to give effect to the Commission's powers under § 7(c), the courts adopted a broad construction of the jurisdictional provisions of the NGA, giving the Federal Power Commission ("FPC") authority to regulate transportation in connection with direct industrial sales.

The natural gas cases, which are rooted in the history and structure of the NGA, do not establish that FERC's interpretation of the FPA was unreasonable. The FPA has its own distinctive history, which has left the regulation of all aspects of bundled retail sales to the States. In this light, it was reasonable for FERC to conclude that transmissions bundled with retail sales are outside of its jurisdiction. FERC's reasonable interpretation deserves judicial deference.

Finally, Enron makes a policy argument that FERC jurisdiction over bundled retail sales is needed to combat discrimination by transmission-owning utilities against their competitors. However, Enron fails to acknowledge that, in states where only bundled service is provided, there is no competition for retail customers. Moreover, there is no discrimination when a utility with an obligation to serve reserves transmission capacity to serve its native load customers. Insofar as Enron and its *amici* are complaining that some utilities may have over-reserved capacity, FERC has authority under Order No. 888 to review and remedy such abuses.

ARGUMENT

I. FERC LAWFULLY ASSUMED JURISDICTION OVER UNBUNDLED INTERSTATE TRANSMISSION SERVICE PROVIDED TO RETAIL CUSTOMERS.

The Commission's conclusion that it had jurisdiction over the transmission component of an unbundled retail sale rests

directly on the language of the Federal Power Act. Its reasoning proceeds in two simple steps.

First, the Commission has jurisdiction over the transmission of electricity in interstate commerce. Transmission of electric energy to retail customers over the interconnected grid is interstate. Thus, unless a specific exception within the statute prevents the Commission from exercising that jurisdiction, the Commission has power to regulate such transmission.

Second, there is no exception in the language of § 201 that would prevent the Commission from assuming jurisdiction over interstate transmission that is unbundled from a retail sale. To be sure, the Commission does not have jurisdiction over a retail "sale of electric energy" under the proviso of § 201(b). However, the separate sale of transmission service is *not* a sale of electric energy and hence does not fall within this exception. Thus, the Commission has soundly concluded that it has jurisdiction over all forms of unbundled, interstate transmission.

A. The Rule Properly Applies to Transmission in Interstate Commerce.

As the court of appeals pointed out, "[b]oth FPA § 201(a) and (b) clearly and unambiguously confer upon FERC jurisdiction over the 'transmission of electric energy in interstate commerce.'" Pet. App. 32a. Consistent with these provisions, in Order No. 888, the Commission applied its rule only to "the transmission of electric energy in interstate commerce . . . ." 18 C.F.R. § 35.28(c)(2) (2000). In the course of the rulemaking proceeding, moreover, the Commission explained that retail transmission on the interconnected grid generally falls within this phrase:

> The term does not turn on whether the contract path for a particular power or transmission sale crosses state lines, but rather follows the physical flow of electricity. Because of the highly integrated nature of the electric system, this results in most transmission of electric energy being "in interstate commerce."

Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking, 59 Fed. Reg. 35,274, 35,284 (July 11, 1994). The only exceptions, the Commission later noted, were the purely intrastate transmission systems in Alaska, Hawaii and an isolated portion of Texas. Pet. App. 305a n.541.

The Commission had no need to say more regarding the scope of interstate transmission since it was already settled, both as a matter of law and of fact, that transmission on the interconnected grid was interstate in nature. This Court had repeatedly held that transmission was interstate if any portion of the electrons involved in the transmission originated out of state or departed for another state. *E.g., FPC v. Florida Power & Light Co.*, 404 U.S. 453, 463 (1972); *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 529 (1945) ("Federal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test."). It was also consistent with the Commission's technical understanding that electrons on an interconnected grid do not move in conformity with contractual arrangements, but rather follow the path of least resistance.[8] Thus, the Commission assumed that a rule directed at the "transmission of electric energy in interstate commerce" would necessarily encompass retail transmissions on the interconnected grid.

---

[8] *See* Pet. App. 612a n.144 ("[I]n reality power flows are rarely confined to a designated contract path . . . . [T]he laws of physics . . . cause power . . . to travel along multiple parallel paths and divide itself among those paths along the lines of least resistance.") (citation and quotations omitted).

New York now apparently seeks to challenge that view.[9] It argues that such retail transmission must be intrastate because "most retail electricity transactions involve generators and consumers that are not only in the same state, but in proximity." Brief of New York in No. 00-568 ("NY Br.") at 37. Then it offers an interpretation of § 201(c) that transmissions are not interstate if they are between buyers and sellers in the same state. *Id.*

To the extent that the generalizations in the Commission's preambles are reviewable at all,[10] New York has failed to present its contentions in a timely fashion. New York failed to challenge the factual adequacy of the rulemaking record in any of the proceedings below. It did not argue before the Commission that the record lacked substantial evidence to support the premise that retail transmission over the interconnected grid could be "in interstate commerce." Nor did it make that contention in the court of appeals.

Under these circumstances, New York has waived the attack it presses here. Under § 313(b) of the Federal Power Act, New York was required to raise that issue before the Commission in its petition for rehearing prior to court review. 16 U.S.C. § 825*l*(b) ("No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the

---

[9] New York's presentation of this issue is, at best, equivocal. The question in its petition referred to "transmission of energy from generators to retail customers *in the same state*" and to "intrastate" retail transmission, New York Pet. for Cert. at i. However, the question in New York's merits brief does not have either reference. Brief of New York in No. 00-568, at i.

[10] *See Kennecott Utah Copper Corp. v. U.S. Dep't of Interior*, 88 F.3d 1191, 1223 (D.C. Cir. 1996) (preamble reviewable only where it has "independent legal effect, which in turn is a function of the agency's intention to bind either itself or regulated parties."); *Florida Power & Light Co. v. EPA*, 145 F.3d 1414, 1418-20 (D.C. Cir. 1998) (denying review of preamble).

application for rehearing unless there is reasonable ground for failure so to do."). *See City of Orville v. FERC*, 147 F.3d 979, 990 & n.13 (D.C. Cir. 1998); *Gulf States Utils. Co. v. FERC*, 1 F.3d 288, 291-92 (5th Cir. 1993); *cf. FPC v. Colorado Interstate Gas Co.*, 348 U.S. 492, 498-99 (1955) (construing analogous provision in § 19(b) of the Natural Gas Act).[11]

New York's failure to raise its issue as to the scope of "in interstate commerce" before the Commission makes it impossible, as a practical matter, for courts to undertake judicial review of that issue. In its two briefs, New York has relied entirely on materials outside of the rulemaking record. *See* NY Br. at 45 n.28; Brief of New York as Respondents in No. 00-809 ("NY Resp. Br.") at 25-26. Neither the Commission nor the other parties to the rulemaking had any opportunity to address New York's points in that context through factual material or otherwise. This is not the forum in which to begin a scientific debate as to the flow of electrons on the interstate grid. In fact, in interpreting parallel statutory language, this Court has ruled that when a party fails to present its issue to the Commission, the court of appeals may not even decide it *sua sponte*. *FPC v. Colorado Interstate Gas Co.*, 348 U.S. at 498-99.

In any event, there is no merit to New York's position. The salient principle of *FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972), is that the potential for commingling of electrons among interconnected systems is sufficient to demonstrate the interstate nature of the transmissions. The Court did not limit the scope of its holding to accounting

---

[11] Even in the court of appeals, New York did not raise the largely factual issues that it is raising now. On the contrary, it acknowledged in that court that "[t]he issue here is a question of law." Brief of Petitioners/Intervenors Public Service Commissions of New York and Florida, *et al.*, at 11 n.14 (Aug. 19, 1999), *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000) (No. 97-1715).

requirements, and no court has construed it as such. *See, e.g., FERC v. Mississippi*, 456 U.S. 742, 757 (1982). Subsequent cases have consistently observed that it is impossible to know the source or destination of individual electrons, and have therefore accepted that transmission over the grid involves interstate commerce. *E.g., Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 381 (1983); *New England Power Co. v. New Hampshire*, 455 U.S. 331, 336 (1982).

Here, New York asserts that retail customers receive most of their energy from the nearest power plant, but does not purport to show that generation from other sources plays no part in serving them. Indeed, New York acknowledges as "arguably accurate" the assumption that all transactions affect the entire grid and admits it is "technically correct" that electrons added to the grid will travel throughout. NY Resp. Br. at 25. Yet this Court has held that the amount of electricity flowing in interstate commerce is irrelevant. *Connecticut Light & Power*, 324 U.S. at 536; *Florida Power & Light*, 404 U.S. at 463. Thus, the admitted possibility that electrons flowed into or out of the state is a sufficient basis to find transmission "in interstate commerce."

New York's argument is ultimately based on a mistaken interpretation of FPA § 201(c). In its view, that subsection "states that transmissions are *not* interstate if they are between buyers and sellers in the same state." NY Br. at 37. But this provision does not refer to "buyers" and "sellers" at all: "For the purpose of this subchapter, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof . . . ." 16 U.S.C. § 824(c). In view of the interconnected nature of the grid and the multiple, non-contractual paths followed by power flows, the Commission could reasonably find that some of the electrons reaching a retail buyer of electric power

originated outside of the buyer's state.[12] Thus, this case must be decided on the Commission's premise that transmission service for unbundled retail sales on the interstate grid involves "the transmission of electric energy in interstate commerce." 16 U.S.C. § 824(b).

B. Transmission Unbundled From a Retail Sale Does Not Fall Within Any of the Exceptions to Section 201(b).

The grant of jurisdiction in FPA § 201(b) for transmission in interstate commerce is not limited by any exception that would preclude FERC from asserting jurisdiction over unbundled retail transmission. FERC found, and the court of appeals agreed, that this grant was not limited to transmission in the course of wholesale transactions. Pet. App. 34a, 305a, 333a. FERC observed that § 201(b) contained two separate grants of jurisdiction that differed in scope—one for the "transmission of electric energy in interstate commerce" and the other for "the sale of electric energy at wholesale in interstate commerce." Pet. App. 333a; *see also* Pet. App. 305a. The first grant for interstate transmission stands in contrast to the second, which the statute specifically limits to

---

[12] Moreover, the distinction between "intrastate" and "interstate" transmission proposed by New York based on its interpretation of FPA § 201(c) is unworkable. Under current retail access programs, electric suppliers do not typically identify the source of their power by reference to a particular generating plant. Rather, they typically acquire a portfolio of generating resources that they can use to supply their overall load requirements. These portfolios include contracts for system power and contracts with other marketers that are selling out of their own portfolios. In many areas of the country, moreover, utilities have formed multi-state power pools in which sources of supply are centrally sold and purchased on a regional basis without identification of generation sources to individual states. In short, New York has not explained how it would even be possible to implement the proposed distinction between interstate and intrastate transmission transactions under its interpretation of § 201(c).

sales "at wholesale." This omission of the reference to "at wholesale" strongly indicates an intent not to limit FERC's jurisdiction over transmission service to wholesale transactions.

This intent is underlined by the one portion of § 201(b) specifically addressing retail transactions. Section 201(b) not only grants jurisdiction over wholesale transactions, but denies any federal jurisdiction over retail sales of electric energy: "The provisions of this subchapter . . . shall not apply to any other sale of electric energy. . . ." 16 U.S.C. § 824(b). The language of this proviso plainly pertains to a sale *of electric energy*. It is this form of retail transaction that is placed outside the Commission's jurisdiction. The proviso by its express terms does not apply to a sale of *transmission service*.

New York cannot turn a sale of unbundled transmission service into a sale of energy by calling unbundling a mere accounting convention. *See, e.g.*, NY Br. at 8 ("Unbundling is a change in bill format."). The heart of unbundling is that each service may be purchased without the other, enabling competition.[13] When transmission is unbundled, it is available from the transmission owner without purchasing its energy at all.[14] Thus, the furnishing of unbundled transmission service is not a "sale of electric energy" within the proviso to § 201(b).

---

[13] *See, e.g.*, Conn. Gen. Stat. §§ 16-244b, 244e ("All customers of electric distribution companies . . . shall have the opportunity to purchase electric generation services from their choice of electric suppliers . . . in a competitive generation market . . . ."); Del. Code Ann. Tit. 26 § 1003; Me. Rev. Stat. Ann. Tit. 35-A § 3202; Okla. Stat. Ann. Tit. 17 § 190.4; Va. Code Ann. § 56-577. *Cf. Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 284 (1997) (describing unbundling of natural gas).

[14] New York admits, "Unbundling . . . allows customers the option of obtaining one or more retail service elements from competitive providers, instead of the utility." NY Br. at 9 (footnote omitted).

Rather than discuss this operative language, however, New York discusses at length the declaration of policy in FPA § 201(a). In essence, New York would have this Court avoid the plain language of § 201(b) by interpreting § 201(a) as imposing an "at wholesale" qualification to the "transmission of electric energy" language. This effort at reconstruction of the statute should be rejected.

First, FPA § 201(a) is a declaration of policy, not a substantive provision of the statute. *See* 16 U.S.C. § 824(a) ("It is declared that . . . ."). Thus, this Court's cases have consistently held that § 201(a) cannot trump specific language in § 201(b). *See Connecticut Light & Power*, 324 U.S. at 527 (holding § 201(a) "cannot nullify a clear and specific grant of jurisdiction, even if the particular grant seems inconsistent with the broadly expressed purpose."); *FPC v. Southern Cal. Edison Co.*, 376 U.S. 205, 215 (1964).

Second, even viewing § 201 as a saving clause, it does not provide the States with jurisdiction over a new service like unbundled retail transmission. Section 201(a) of the FPA states in pertinent part that "Federal regulation . . . [is] to extend only to those matters which are not subject to regulation by the States." 16 U.S.C. § 824(a). At most this suggests that the States would continue to regulate those matters that they were then regulating. Interstate transmission unbundled from a retail sale of energy was not among the transactions regulated by the States in 1935 and therefore was not "saved" by this provision. *See Knickerbocker Ice Co. v. Stewart*, 253 U.S. 149, 162 (1920) ("[t]he usual function of a saving clause is to preserve something from immediate interference—not to create"); *Gorbach v. Reno*, 219 F.3d 1087, 1094 (9th Cir. 2000) (*en banc*) ("Under the saving clause, what authority the Attorney General has, she keeps, but it does not give her more.").

Even taking the most aggressive interpretation of FPA § 201(a)—that it reflected a policy of giving the States

jurisdiction over any area that they *could* regulate—it would not have encompassed unbundled interstate transmission. The scope of what Congress believed the States could regulate would be measured by the relevant constitutional law that existed at the time of enactment. *See FPC v. East Ohio Gas Co.*, 338 U.S. 464, 472 (1950) ("*[P]rior* constitutional decisions, not what we have since decided or would decide today, form the measure of the gap which Congress intended to close by this Act."); *Phillips Petroleum Co. v. State of Wisconsin*, 347 U.S. 672, 684 (1954). In 1935, state regulation of interstate transmission distinct from a sale of electric power would have been viewed as a "direct" regulation of interstate commerce, and hence impermissible under the dormant Commerce Clause.

Mill Creek Coal & Coke Co. v. Public Service Commission, 100 S.E. 557 (W. Va. 1919), a case later cited by this Court in *Attleboro*, illustrates this point. *Mill Creek Coal* involved a Virginia hydro-electric company selling electric power directly to consumers in West Virginia. *Id.* at 560-61. The court stressed the distinction between the sale of electric power and the independent sale of transmission: "The vital distinction should be noted between regulation of rates of transportation and of the rates at which a commodity shall be sold." *Id.* at 562. The court recognized that rates of transportation invoked matters of "national importance requiring uniformity of regulation respecting the rates thereof, and hence [are] usually beyond the regulatory power of the state." *Id.* Nevertheless, when transmission is sold to the retail customer as part of the price of the commodity, the state's regulatory interests are elevated: "The price at which a commodity is sold is essentially local, affecting chiefly those in the community where it is made, and only incidentally, if at all, touching those outside of the

community." *Id.* Thus, the court held, the sale of the delivered commodity was subject to state regulation.[15]

This Court's precedents just prior to passage of the FPA reflect the same thinking. Thus, in *Public Utilities Commission of Rhode Island v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927), this Court cited *Mill Creek Coal* for the concept that "transmission of electric current from one state to another, like that of gas, is interstate commerce." *Attleboro*, 273 U.S. at 86. The Court reasoned that state regulation of an interstate wholesale sale of electricity was impermissible as a "direct burden upon interstate commerce." *Id.* at 89.[16] Thus, under the law at the time of enactment of the FPA, transmission unbundled from a retail sale would likely have been viewed as outside the states' regulatory power, since such state regulation would have been viewed as a "direct" rather than incidental burden on interstate commerce.

In view of this state of the law at the time of enactment, the policy declaration in § 201(a) would not help New York's case. The states never exercised authority to regulate the

---

[15] *Mill Creek Coal*'s reasoning is consistent with the Court's existing precedents holding that the direct regulation of transportation between States fell within the exclusive power of the federal government. *See South Covington & Cincinnati St. Ry. v. City of Covington*, 235 U.S. 537, 545-48 (1915); *Wabash St. L. & P. Ry. v. State of Illinois*, 118 U.S. 557, 573-77 (1886).

[16] On the other hand, the interstate transmission involved in the bundled transaction in *Pennsylvania Gas Co. v. Public Service Commission*, 252 U.S. 23 (1920), was viewed as distinguishable on the ground that it was part of the "furnishing of gas" to local consumers. *Attleboro*, 273 U.S. at 87-88. "In holding that the New York Public Service Commission might regulate the rate charged to these consumers, the court said that while a state may not 'directly' regulate or burden interstate commerce, it may in some instances, until the subject matter is regulated by Congress, pass laws 'indirectly' affecting such commerce, when needed to protect or regulate matters of local interest . . . ." *Id.* at 87.

transmission sold independently of the sale of electricity and could not have done so if they tried. New York's effort to invoke the declaration of policy to achieve an *expanding* reservation of jurisdiction to the states runs counter to this Court's precedents interpreting the FPA, which have insisted that the lines drawn by that statute do not change in light of evolving constitutional standards. *Arkansas Elec. Coop. Corp.*, 461 U.S. at 380; *Southern California Edison*, 376 U.S. at 213-17. The policy declaration in § 201(a) does not override the specific grant of jurisdiction over interstate transmission.

C. The Legislative History Does Not Contradict The Plain Language Used In the Statute.

New York emphasizes various forms of legislative history as an antidote to the statutory language. It cites snippets from hearings, debates, and committee reports, as well as subsequent legislative history and litigation positions. Such legislative history is not relevant in the interpretation of an unambiguous statute.[17] Congress has granted jurisdiction over transmission in interstate commerce, except where that function is an inseparable part of a direct sale of electric energy. No resort to the legislative history is necessary or appropriate.

Even if resort to legislative history were permissible, however, *this* legislative history would not be of any assistance. In Order No. 888, FERC was addressing a new phenomenon—unbundled transmission at the retail level—which did not exist at the time of enactment of the FPA. No one in Congress in 1935 could have formed or expressed an intent as to how this new product should be handled, and no

[17] *Davis v. Michigan Dep't of the Treasury*, 489 U.S. 803, 808 n.3 (1989) ("Legislative history is irrelevant to the interpretation of an unambiguous statute."); *Russello v. United States*, 464 U.S. 16, 23 (1983); *United States v. Oregon*, 366 U.S. 643, 648 (1961).

one did. Thus, even some of the parties signing the New York brief told the Commission that the legislative history is inconclusive.[18] The Commission concluded that the legislative history did not speak directly to the issue at hand. *See* Open Access NOPR, 60 Fed. Reg. 17,662, 17,713 (Apr. 7, 1995).

In fact, the legislative history provides at least as much support for the Commission's interpretation of the statute as for that urged by petitioners. In the first place, as New York itself points out, legislators were concerned that "Congress might inadvertently empower FERC to preempt *pre-existing* state regulation." NY Br. at 20 (emphasis added). *See also* NY Br. at 23 ("The Reports repeatedly stated that the proposed legislation safeguarded all aspects *of pre-existing* state regulation.") (emphasis added); NY Br. at 28, *quoting* FPC Commissioner Seavey ("everything is left to the state commissions that they are performing now"). Such pre-existing state regulation encompassed only the regulation of bundled retail sales, which FERC has preserved.

Second, New York cites several statements in the legislative history suggesting that Congress did not intend to confer FERC jurisdiction over retail sales. NY Br. at 21. As noted earlier, however, this intent is effectuated by the language of FPA § 201(b), which prohibits federal authority over "any other sale of electric energy"—language that does not address interstate transmission sold independently of electric energy. Similarly, California points to various statements indicating that Congress intended to "adopt" this

[18] *See* Request of the National Association of Regulatory Utility Commissioners for Rehearing of Order No. 888, at 5 ("we agree that the legislative history is not helpful in resolving this jurisdictional question") (May 24, 1996) (FERC Docket Nos. RM95-8-00 and RM94-7-001); Request of the Staff of the Virginia State Corporation Commission for Rehearing of Order No. 888, at 4 ("The legislative history of the FPA does not resolve this jurisdictional question . . . .") (May 23, 1996) (FERC Docket Nos. RM95-8-00 and RM94-7-001).

Court's decision in *Pennsylvania Gas Co. v. Public Service Commission*, 252 U.S. 23 (1920). Calif. Br. at 8-11. But the heart of that case was a sale of delivered (*i.e.*, bundled) electricity to the retail customer. Thus, even Solicitor DeVane's statement, as quoted by California, reveals the necessity for a sale as a predicate for jurisdiction under the retail sale proviso. *See* Calif. Br. at 10-11 ("This bill does not give the Commission jurisdiction over *energy* that is transmitted in interstate commerce by a particular company and *sold by that company* to consumers.") (emphasis added). These and other statements regarding "rates" for retail sales must be read in their historical context, when all retail sales involved bundled delivery of energy.

Third, the states are not helped by legislative history indicating that Congress was seeking to fill the jurisdictional void left by this Court's *Attleboro* decision. That history may illuminate the distinction drawn in the statute between wholesale transactions in interstate commerce and "any other sale of electric energy," but it does not explain Congress' enactment of a separate head of jurisdiction for "transmission of electric energy in interstate commerce. . . ." 16 U.S.C. § 824(b). Even in 1935, Congress was aware of an increasing amount of interstate transmission that would not be subject to state regulation. *See* 79 Cong. Rec. 10,352, 10,377 (June 28, 1935) (volume of interstate transmission was "constantly growing and will increase indefinitely in time and amount.") (statement of Rep. Lea). Thus, the legislation was worded "to make plain that it includes interstate transmission where there is no sale . . . ." S. Rep. No. 74-621, at 19 (1935).

Indeed, even though *Attleboro* involved a wholesale transaction, it cited *Mill Creek Coal* for the proposition that the transmission of energy across state lines was interstate commerce. As noted above, state regulation of interstate transmission in the absence of a retail sale of energy would have been problematic under the Commerce Clause. *Cf. Mill Creek Coal*, 100 S.E. at 562 ("Because of the very nature of

the subject-matter conflicting state regulations respecting [transmission] rates ordinarily would result in discord and chaos."). Congress knew of the "comparatively recent transformation [of the electric industry] from an industry of a purely local character to one of a dual local and national character."[19] There was thus good reason for Congress to make a separate provision for federal authority over the transmission of electric energy in interstate commerce.

This grant becomes particularly relevant when states restructure retail service for competition and thereby permit participation by energy suppliers in an interstate market. Out-of-state generators competing for those retail customers need equal access to transmission in order to provide competitive service. Yet individual states are not well situated to regulate unbundled interstate transmission. Once a state's retail markets are opened to out-of-state competition, its interests as a regulator of the incumbent utility may conflict with those of other states whose generators are interested in serving those same retail customers. *See Arkansas Elec. Coop. Corp.*, 461 U.S. at 377 ("[T]he production and transmission of energy is an activity particularly likely to affect more than one State, and its effect on interstate commerce is often significant enough that uncontrolled regulation by the States can patently interfere with broader national interests."). Thus, when a state chooses to unbundle retail service and opens its doors to retail competition, the FPA permits the transmission network to be managed on a regional or national level.[20]

---

[19] *Public Utility Holding Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce*, 74th Cong. 797 (1935) (Memorandum of Oswald Ryan, FPC General Counsel, and Dozier A. DeVane, FPC Solicitor).

[20] *Cf. Gulf States Utils. Co. v. FPC*, 411 U.S. 747, 758 (1973) (a primary purpose of the FPA was to "provide effective federal regulation of the expanding business of transmitting and selling electric power in interstate commerce."); *Appalachian Power Co. v. Pub. Serv. Comm'n. of West Virginia*, 812 F.2d 898, 904-05 (4th Cir. 1987).

D. New York Cannot Defeat the Language of the Statute By Reliance On Presumptions Regarding Preemption.

Finally, New York cannot defeat federal jurisdiction over unbundled retail transmission by invoking a presumption against federal preemption of traditional state powers. *See* NY Br. at 13-17. Preemption analysis focuses on the impact of a defined federal regulatory scheme on state laws in the same or a related field.[21] Here, the preemptive effect of the federal scheme is clear: if FERC has jurisdiction of a form of transmission, that jurisdiction is exclusive. *See Mississippi Power & Light Co. v. Mississippi*, 487 U.S. 354, 377 (1988) (Scalia, J., concurring) ("It is common ground that if FERC has jurisdiction over a subject, the States cannot have jurisdiction over the same subject."). Thus, the question here is not what provision Congress has made for preemption, but what jurisdiction Congress granted in the first instance in the agency's organic statute. None of the cases cited by New York for its presumption deal with jurisdictional questions of that kind, and this Court has not applied that presumption in interpreting grants of authority to federal agencies.[22]

---

[21] Thus, in each of the classic preemption cases cited by New York, it was not the scope of the federal officials' power to which the presumption was applied, but rather to the question whether concurrent state regulation was displaced. *See, e.g., Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218 (1947) (Federal Warehouse Act preemptive of similar state regulation); *Jones v. Rath Packing Co.*, 430 U.S. 519 (1977) (whether Federal Meat Inspection Act displaces state labeling law); *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504 (1992) (whether federal tobacco labeling requirement preempts state tort action).

[22] *Cf. Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 743-44 (1996) (finding presumptions against preemption do not apply to issues concerning the substantive meaning of statutes, even if one proposed meaning results in greater preemption than another).

This is categorically true with respect to the Federal Power Act. In FPA § 201, Congress provided specific instructions as to the scope of federal jurisdiction.[23] While this Court has analyzed the scope of that section at least nine times, *not a single one* of this Court's decisions has relied on a presumption in favor of state police powers as a tool in that analysis. In each case, the Court has approached the statute based on its own terms, rather than an exogenous assumption about congressional intent to preempt.

In any event, federal jurisdiction over unbundled interstate transmission does not involve an encroachment on the State's traditional police powers. The States have *never* regulated (and most likely could not regulate) interstate transmission severed from the sale of electricity. The presumption against federal preemption cited by New York has no role with respect to this new service and the new interstate markets in which it will be offered.

Finally, FERC's interpretation of § 201(b) does not leave the States without authority over matters of primarily local concern. New York does not articulate, and it is difficult to conceptualize, how the Commission's jurisdictional decision has harmed these petitioners. Even where states have introduced competition, they nevertheless retain jurisdiction over all retail energy sales, all local distribution facilities (whose extent will be based on their own recommendations); all transactions of municipalities; and over all generation and transmission siting. Moreover, it is only where states have, subsequent to Order No. 888, chosen to restructure their retail markets that retail transmission would fall under federal jurisdiction. Order No. 888 does not intrude unduly into local matters or significantly alter the federal-state balance.

---

[23] *Cf. Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 376 n.5 (1986) (Communications Act "presents its own specific instructions regarding the correct approach to the statute").

E. All Retail Transmission Does Not Fall Under The Exception for Local Distribution.

Amicus California presses for reversal on a completely different ground than that urged by New York. California acknowledges that § 201(b) confers FERC jurisdiction over interstate transmission, but it argues that all retail transmission is exempt from FERC regulation under the exception for "local distribution" facilities in § 201(b). In Order No. 888, FERC interpreted the "local distribution" proviso and adopted a fact-based, seven-factor test for determining whether a facility functions primarily as a local distribution facility subject to state jurisdiction. Pet. App. 282a-283a. California now effectively attacks the validity of that test, arguing that all unbundled retail transmission constitutes "local distribution" under § 201(b).

California's argument is not properly before this Court. California did not appear as either a party or an amicus in the proceedings below. Petitioner New York did not present California's issue before FERC[24] and did not attack the seven-factor test at all before the court of appeals. On the contrary, in the court of appeals, New York *endorsed* the seven-factor test as a means of defining "local distribution" and argued that it should be applied to wholesale transactions as well as retail ones.[25] The court of appeals addressed and

[24] The argument made by California is barred by FPA § 313(b) because it was never presented to the Commission in a petition for rehearing by a party in these proceedings. Before FERC, New York argued that only two of the seven factors should be used to identify local distribution in large metropolitan and remote rural areas. New York Motion for Rehearing of Order No. 888, at 18-19 (May 24, 1996) (FERC Docket Nos. RM95-8-00 and RM94-7-001). New York did not pursue this challenge in the court of appeals.

[25] *See* Brief of Petitioners/Intervenors Public Service Commissions of New York and Florida, *et al.*, at 31 (Aug. 19, 1999), *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000) (No. 97-1715) ("The seven-indicator test established in FERC Order 888

rejected this complaint. Pet. App. 37a-39a. New York then raised its effort to expand the use of the seven-factor test in its petition for certiorari to this Court, but even this issue regarding local distribution was not accepted for review. In these circumstances, California, as amicus, cannot introduce before this Court a completely different attack on the Commission's rulemaking that has never been presented to any tribunal in the proceedings below.[26]

In any event, FERC's reading is faithful to the statutory text, giving meaning to all of the proviso's language. The phrase "facilities used in local distribution" delineates an exception to the Commission's jurisdiction over facilities used for jurisdictional transmission and sales. California's reading would make redundant the exception for "any other sales of electric power," since, in its view, all aspects of retail sales, including unbundled transmission, fall within the exception for local distribution. Yet § 201(b) identifies "local distribution" as a *separate* exception. Congress presumably intended it to have a separate, more narrow meaning than the retail sales proviso.

That meaning is apparent upon examination of the case law available to the Congress that enacted the FPA. This Court had held in *East Ohio Gas Co. v. Tax Comm'n of Ohio*, 283 U.S. 465 (1931), that interstate movement of natural gas had ended, for tax purposes, when it was stepped down in pressure and divided into the many small service lines that connected with the pipes on the consumers' premises. This

represents FERC's current judgment as to what constitutes local distribution, and should be applied in all instances to define the local distribution facilities subject to state regulation rather than federal.") (footnote omitted).

[26] This Court will not consider an argument advanced by amicus when it was not raised or passed on below and is not advanced in this Court by the party on whose behalf the argument is being raised. *See United Parcel Serv., Inc. v. Mitchell*, 451 U.S. 56, 60 n.2 (1981).

was viewed as analogous to the "breaking of an original package." *Id.* at 471. Thus, "local distribution" did not refer to an entire "retail sale" but to the point in the process of delivery where interstate shipment was thought to end. *Id.* at 472.

This doctrine was promptly applied to the distribution of electric power. "While electric current can hardly be said to 'come to rest' within the state, its interstate journey ends at the transformer which uses it for the production of low voltage currents for use within the state. The situation is the same in principle as the breaking up of an original package . . . ." *South Carolina Power Co. v. South Carolina Tax Comm'n*, 52 F.2d 515, 525 (E.D.S.C. 1931) (cited in the 1935 Senate Hearings at 802), *aff'd*, 286 U.S. 525 (1932).

Shortly thereafter, Congress enacted the FPA, with its language exempting "local distribution" facilities in § 201(b). In *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515 (1945), this Court confirmed that this phrase would be interpreted consistently with the basic standard of *East Ohio Gas*, but adapted to fit the peculiarities of electrical transmission. The question there was whether facilities used to "step down" the voltage were local distribution facilities. The Court found that its prior holding that "distributing gas at low pressure to consumers is a local business" did not address the question whether "the process of reducing energy from high to low voltage in subdividing it to serve ultimate customers" was also "local distribution." *Id.* at 534. Thus, the Court remanded this issue to the Commission for what was viewed as a factual determination.[27] The Court never adopted any holding that all retail sales were covered by the local distribution exemption.

---

[27] *See Connecticut Light & Power*, 324 U.S. at 534-35 ("It is not for us to make an original appraisal of the facts. We do not therefore undertake to decide as an original matter whether the facilities in question are or are not facilities which can subject the Company to the act.").

Again in *FPC v. Southern California Edison Co.*, 376 U.S. 205, 210 n.6 (1964), this Court observed that whether facilities are used in local distribution "involves a question of fact to be decided by the FPC as an original matter." There, the Court sustained the Commission's finding that certain retail sales at high voltage to industrial customers were not local distribution. With support in the record, the Court reasoned, "the conclusion may properly rest upon the specialized experience of the FPC in determining such questions." *Id.* at 210. Other decisions of this Court have similarly treated the phrase "local distribution facilities" as determined by the physical characteristics of the electrical or gas lines, rather than the presence of a retail transaction.[28]

Thus, FERC acted well within existing precedent when it promulgated a rule seeking to define "local distribution" based on the physical characteristics of the facilities, such as the voltage and the role of the lines in directing energy to an end use. *See* note 4, *supra*. Neither *amicus* California nor any party has shown that rule to be arbitrary and capricious. Thus, unbundled retail transmissions are not excepted from the Commission's jurisdiction by virtue of the exception for "local distribution facilities."

Finally, California attempts to rely on its own well known problems with power supply as a reason for this Court to reject FERC's jurisdictional rule. Calif. Br. at 1-2, 27. California offers no support for its assertion that its recent problems were caused by FERC's assertion of jurisdiction over unbundled retail transmission. With or without such

---

[28] *See United States v. Public Utilities Comm'n of Cal.*, 345 U.S. 295, 316 (1953) ("[T]he facilities supplied 'local distribution' only after the current was subdivided for individual consumers."); *East Ohio Gas Co.*, 338 U.S. at 469-70 ("[W]hat Congress must have meant by 'facilities' for 'local distribution' was equipment for distributing gas among consumers within a particular local community, not the high-pressure pipe lines transporting the gas to the local mains.").

jurisdiction, FERC would still possess authority over all wholesale transactions in the state and would still lack authority over bundled retail sales. California's problems are severe, but they are not related to the Commission's assertion of jurisdiction over the specific category of transmission lines used in unbundled retail sales.[29] California's recent troubles do not change the legal analysis here.

II. FERC LAWFULLY DECLINED TO ASSERT JURISDICTION OVER TRANSMISSION THAT IS BUNDLED WITH A RETAIL SALE.

In Order No. 888, FERC limited its jurisdiction at the retail level to interstate transmission that occurs when states direct or permit utilities to unbundle their services. FERC therefore preserved State jurisdiction over bundled retail transmission that had been exercised before the FPA was enacted and that has continued to be exercised for the last 65 years under the FPA. Enron now seeks to displace this established regulatory scheme, arguing that FERC should have exercised exclusive jurisdiction over *all* transmission at the retail level even if bundled with a retail sale.

The reach of this assertion is breathtaking. Enron's position means that for the five or more decades since the interstate nature of transmission on the grid has been established, FERC has been failing in its duty to regulate the transmission component of bundled retail sales; all state commissions have been erroneously asserting jurisdiction over the transmission aspect of such sales; and all reviewing courts have erred in failing to recognize and enforce this distinction. Enron's position would also require all existing

[29] For example, California's approach would not alter FERC's authority to regulate the Independent System Operator ("ISO"), because FERC has jurisdiction over wholesale transactions, including unbundled wholesale transmissions, for which the ISO is primarily responsible.

bundled retail rates to be unbundled and re-established, an enormous undertaking.

In viewing transmission for a bundled sale as part and parcel of the retail sale, FERC adopted a reasonable interpretation of the statutory language, which accords with the history of operation under the statute. FERC also limited the scope of its mandatory open access tariff to those markets in which it is needed: those in which transmission owners are competing against generators for the same retail customers. If there is any ambiguity in the statute, FERC's interpetation should be upheld as a reasonable construction entitled to judicial deference.

A. Enron Ignores Statutory Language That Preserves Pre-Existing State Jurisdiction Over Bundled Retail Sales.

Section 201(b) reserves to the States jurisdiction over all retail sales of electricity. Under that provision, the Act applies to interstate transmission or wholesale sales of electric energy but not "to any other sale of electric energy." 16 U.S.C. § 824(b). FERC reasonably viewed transmission bundled in a retail sale as an integral component of that sale of energy. It therefore properly refrained from taking jurisdiction in light of the express terms of the proviso.

Enron does not challenge the Commission's characterization of bundled transmission. In fact, Enron admits that the transmissions for which it seeks federal jurisdiction are "components of a bundled retail sale . . . legally as well as factually." Enron Br. at 18. Given a proviso that expressly excludes "any other sale of electric energy," this admission should be fatal.

Enron would apparently read this proviso out of the statute. Neither its opening nor its responsive brief mentions it. Enron reasons: "Transmission of energy across state borders does not cease to be interstate transmission merely because it

is bundled with a sale of energy as an invoicing matter." Enron Br. at 18.

This reasoning is flawed at its core. The question is not whether a transmission ceases to be interstate, but rather whether, as a component of a bundled sale, it is excluded under the terms of a proviso that carves out "any other sale of electric energy." Order No. 888 gives meaning to that language because it finds that a transmission service that might otherwise meet a jurisdictional requirement (interstate transmission) is *excluded* from FERC jurisdiction. This reading gives effect to all of the language in the statute. Otherwise, the "other sale" proviso would have no purpose. It would redundantly exclude the very same non-wholesale sales that are left out of § 201(b)'s jurisdictional grant.

Moreover, like New York, Enron is wrong to characterize the bundling of retail sales as only an "invoicing matter." When transmission is bundled in a retail sale, there is not only a single price, but also a single product—delivered energy. The consumer can buy only that product and only from one utility in a single transaction. The utility's delivery of the energy to the consumer is thus an inseparable aspect of the utility's "sale of electric energy" within the meaning of the proviso to § 201(b). As FERC stated, "we believe that when transmission is sold at retail as part and parcel of the delivered product called electric energy, the transaction is a sale of electric energy at retail." Pet. App. at 306a.

FERC's interpretation not only gives meaning to the proviso of § 201(b); it also fits well with the declaration in § 201(a), which reserved to the States their preexisting regulatory jurisdiction. In 1935, there were already a substantial number of bundled retail sales involving what was found to be interstate transmission within the State's regulatory authority. *Mill Creek Coal,* like *Pennsylvania Gas* in the natural gas area, exemplified this phenomenon.

Congress clearly intended to give regulation of such sales to the States.

The legislative record surrounding the 1935 Act confirms this point. It shows that Congress intended to preserve existing state authority over bundled retail sales of electric power, including those that involved interstate transmission over an integrated system. Both Committee reports state that the bill leaves to the States their authority over retail sales of electric energy, even where that energy is brought in from out of state.[30] In proposing the bill later enacted into the FPA, FPC Solicitor DeVane repeatedly stated during his testimony that the States would retain jurisdiction over bundled retail service even when interstate transmission was involved.[31] While legislative history may be of questionable value in applying a statute to a product or service that was not even known to the enacting Congress (such as unbundled retail transmission), it has force when legislators have specifically considered the situation and consistently expressed their intent.

In the years that followed, FERC never asserted any jurisdiction over the transmission aspects of bundled retail sales[32] and the States universally did

---

[30] *See* S. Rep. No. 74-621, at 48 (1935) ("This subsection leaves to the States the authority to fix local rates even in cases where the energy is brought in from another State."); H.R. Rep. No. 74-1318, at 27 (1935) ("[T]he authority of States to fix local rates is not disturbed even in those cases where the energy is brought in from another State.").

[31] Mr. DeVane made his views explicit in a colloquy with Congressman Monoghan. *See Pub. Util. Holding Cos.: Hearings on H.R. 5423 Before the House Committee on Interstate and Foreign Commerce,* 74th Cong. 521-22 (1935).

[32] Enron concedes that "the Commission heretofore has not exercised its . . . authority to regulate transmission to a retail customer." Application of the Coalition for a Competitive Electric Market for Reconsideration and Clarification or, In the Alternative, Rehearing of

so.[33] This longstanding interpretation by the federal agency charged with administration of the Act is entitled to considerable deference. *E.g., United States v. Cleveland Indians Baseball Co.*, 121 S. Ct. 1433, 1444-45 (2001) (according "substantial" deference to agency's 61-year interpretation); *NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 274-75 (1974).

Moreover, Congress has twice amended the jurisdictional sections of the FPA, but has left alone state regulation of bundled retail sales. *See* PURPA, Pub. L. No. 95-617, Title II, § 204(b), 92 Stat. 3140 (1978); Energy Policy Act, Pub. L. No. 102-486, Title VII, § 714, 106 Stat. 2911 (1992). In these circumstances, Congress has acquiesced in the existing federal-state allocation of jurisdiction over bundled retail sales. *See FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 143-61 (2000); *Bob Jones Univ. v. United States*, 461 U.S. 574, 599-601 (1983).

Indeed, in 1992, Congress enacted amendments to the FPA that confirmed the inability of the Commission to deal with transmission aspects of a bundled retail sale. In § 212(h) of the FPA, Congress precluded FERC from conditioning any of its orders upon or directing "the transmission of electric energy . . . directly to an ultimate consumer." 16 U.S.C. § 824k(h). In effect, FERC was barred from ordering that any utility provide "retail wheeling" — mandatory transmission access to any retail consumer.

Order No. 888, at 5 (May 24, 1996) (FERC Docket Nos. RM95-8-00 and RM94-7-001).

[33] *See, e.g.*, Pet. App. 28a, 30a; *People ex. rel. Horton v. Prendergast*, 162 N.E. 10, 12 (N.Y. 1928); *see also* Hon. Ashley C. Brown, *State Power Over Transmission Access and Pricing: The Giant Will Not Sleep Forever*, 124 Pub. Utils. Fort. 21 (1989) ("State jurisdiction over retail rate making provides for considerable influence over transmission policy. The bulk of transmission pricing is already done by the states in the course of retail ratemaking. ") (*available in* Westlaw TP-ALL).

At the same time, Congress did nothing to disturb the existing state regulation of bundled transmission at the retail level and specifically sought to preserve it. "Nothing in this subsection shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an ultimate consumer." 16 U.S.C. § 824k(h). This section necessarily assumes that States have some degree of authority over transmission to a consumer and would be meaningless if Enron's interpretation of FPA § 201(b) were correct. Where "Congress has not just kept its silence by refusing to overturn the administrative construction, but has ratified it with positive legislation, we cannot but deem that construction virtually conclusive." *CFTC v. Schor*, 478 U.S. 833, 846 (1986) (quotations and citation omitted).

At this point, a rule classifying transmission underlying bundled retail sales as subject to federal jurisdiction would create a huge regulatory burden and uncertainty in the industry. It would require FERC to go back and reset the price for the transmission component of every such retail sale, and then force every State that has not unbundled retail services to establish separate rates for the generation and distribution components of the rates for each utility subject to its jurisdiction. Absent a clear showing of such intent, the statute should not be interpreted to disturb the established federal and state practices governing the regulation of bundled retail sales and to inject such regulatory uncertainty into the industry.

B. The NGA Case Law Does Not Compel a Conclusion That FERC Has Jurisdiction Over Bundled Retail Transmission.

Lacking supporting FPA cases, Enron resorts to the case law delineating FERC's jurisdiction under the Natural Gas Act ("NGA"), such as this Court's decision in *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621 (1972). The

NGA case law, however, though sometimes relevant to interpreting the FPA, is not on-point here, and does not compel the extension of FERC jurisdiction to bundled retail transmission.

As Enron points out, this Court has an "established practice of citing interchangeably decisions interpreting the *pertinent* sections of the two statutes." *Arkansas Louisiana Gas Co v. Hall*, 453 U.S. 571, 577 n.7 (1981) (emphasis added). But the Court has never stated that the *jurisdictional* provisions of the two statutes are interchangeable, and with good reason. Jurisdictional principles under the Natural Gas Act have developed differently in light of the characteristics of the gas industry and the somewhat different structure of that statute. A mechanical appropriation of the law from the NGA to the FPA in the jurisdictional context would be inappropriate.

Congress enacted the jurisdictional provisions of the FPA and NGA against the backdrop of two industries that already had different origins and organizational structures. Electrical generation facilities were typically sited in or near the service territory of the utility, but gas fields had to be exploited where they were found. Most gas had to be transported by pipeline at long distances and across State lines from gas fields located in a few producing areas.[34] Interstate pipelines were therefore widely used to bring gas from producing regions to consuming states. Moreover, the gas industry was characterized by separate ownership of the individual segments of the industry, whereas the electric industry has been historically characterized mostly by vertical ownership and

[34] *See Pennsylvania v. West Virginia*, 262 U.S. 553, 586-87 (1923); *see also Hearings on H.R. 11662 Before House Committee on Interstate and Foreign Commerce*, 74th Cong. 117 (statement of John E. Benton, General Solicitor of Railroad and Utilities Commissioners) ("Thirty-seven States which now use natural gas to a greater or less extent obtain most of that gas, with the exception of six or eight States, outside of their own borders.").

integrated generation of all segments of the business.[35] Thus, interstate transportation was typically handled by companies different from those that handled production and distribution.[36] In effect, in the gas industry, the transportation function had already been unbundled from the retail sale of the gas.

In these circumstances, Congress sought to place all interstate transportation of natural gas under federal control.[37] In § 7 of the NGA, Congress imposed a certification requirement that was intended to work together with FERC's jurisdiction under NGA § 1(b).[38] NGA § 7(c) requires gas companies to obtain from FERC a certificate of public convenience and necessity before constructing or operating any facility for the transportation or making of any

[35] *See Cities of Aitkin v. FERC*, 704 F.2d 1254, 1257 n.4 (D.C. Cir. 1982) ("the natural gas industry is relatively unintegrated in comparison to the electric industry"); *see also* EDWARD KAHN, ELECTRIC UTILITY PLANNING AND REGULATION 16-21, 306-07 (1988) ("The natural gas industry is substantially less integrated than the electric utilities industry . . . The pipeline companies were the major developers of the gas industry, but they had relatively little corporate connection either to the local distribution companies or the gas suppliers."); JAMES C. BONBRIGHT, ET AL., PRINCIPLES OF PUBLIC UTILITY RATES 622 (1988) ("vertical integration is much less common than in the electric industry").

[36] Kahn, *supra* note 35, at 306-07.

[37] *See Hearings on H.R. 11662 Before House Committee on Interstate and Foreign Commerce*, 74th Cong. 56 (1936) (statement of Dozier A. DeVane, Solicitor, Federal Power Commission) ("The whole purpose of this bill is to bring under Federal regulation the pipe lines and to leave to the State commissions control over distributing companies and over their rates, whether that gas moves in interstate commerce or not.").

[38] *See Hearings on H.R. 11662 Before House Committee on Interstate and Foreign Commerce*, 74th Cong. 435 (statement of Chairman Lea) (1936) ("The gas industry is in a separate position from other utilities. There is greater reason for this provision [NGA § 7(c)] in the case of gas than electricity.").

jurisdictional sale.[39] There is no parallel certification requirement in the FPA.

The Commission and the courts concluded relatively early in the statute's history that the agency would have § 7(c) certificate authority over transportation for "direct sales"—which were typically sales of gas in large volumes and high pressure to industrial customers. *See Panhandle Eastern Pipe Line Co.*, 232 F.2d 467, 471-72 (3d Cir.), *cert. denied*, 352 U.S. 891 (1956). This was consistent with this Court's view that "transportation of natural gas in interstate commerce" encompassed movements in high-pressure pipelines. *East Ohio Gas Co.*, 338 U.S. at 472-73.

It was in this context that this Court decided *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 640-41 (1972). It upheld the Commission's power to curtail direct sales to industrial customers, sales that were already certificated pursuant to § 7 (*see id.* at 624). In order to give effect to the Commission's powers over transportation under § 7, the Court adopted a broad interpretation of the jurisdictional provision of the NGA, permitting the exercise of authority over transportation even when the sales themselves were exempt from FPC jurisdiction. The Court also relied directly on the legislative history of the NGA: "That rate setting was the only subject matter covered by [the exception for] 'sales' . . . is clear from the legislative history of the proviso." 406 U.S. at 639. Because *LP&L* focused on direct industrial sales and rested on the different structure and history of the Natural Gas Act, it is not an accurate guide to the treatment of other forms of retail transmission under the Federal Power Act. *Cf. Algonquin Gas Transmission Co. v. FERC*, 809 F.2d 136,

[39] This Court has also noted, "[T]he initial interest of Congress in regulation of transportation facilities was reemphasized in 1942 by passage of an amendment to § 7(c) of the Act broadening the Commission's powers over the construction or extension of pipe lines." *East Ohio Gas Co.*, 338 U.S. at 468.

142-43 & n.10 (1st Cir. 1987) ("[T]hat two different industries regulated under two different statutes must be treated exactly alike, is utterly unpersuasive.).[40]

If the NGA cases have any relevance here, at most they suggest that § 201(b) is susceptible to another interpretation than FERC adopted. These cases do not *compel* the reading urged by Enron. As the Court of Appeals pointed out, "[a] regulator could reasonably construe transmissions bundled with generation and delivery services and sold to a consumer for a single charge as either transmission services in interstate commerce or as an integral component of a retail sale." Pet. App. 35a. FERC's construction was reasonable in light of the language of the statute and its own distinctive history, which recognizes the role of the states in regulating all aspects of bundled retail sales. FERC's choice among reasonable interpretations is entitled to appropriate deference. *See Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844 (1984) ("[A] court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency.") (footnote omitted).

C. Regulation of Bundled Sales Is Not Necessary to Fulfill the Stated Objectives of Order No. 888.

Enron and its allies argue that, by failing to take jurisdiction over the interstate transmission component of bundled retail service, FERC left in place an unduly

[40] For example, in *LP&L*, this Court explained that curtailment of industrial customers (many of whom had alternative sources of supply) was necessary to assure fairness to residential customers whose sales were already being curtailed and who had no such options. 406 U.S. at 632. Here, Enron would invoke this case to achieve the opposite result—an expansion of federal jurisdiction to encompass bundled sales to residential customers who have no choice, so that Enron may make use of that transmission capacity in its own competitive transactions.

discriminatory situation that is inconsistent with its own stated objectives in issuing Order No. 888. They assert that public utilities have acted discriminatorily in providing transmission services to their own bundled retail customers in comparison with the services that they provide under the Order No. 888 open access tariffs. This argument fails for several reasons.

First, the argument puts the cart before the horse. The question before the Court is whether Congress granted jurisdiction to FERC to regulate the interstate transmission component of bundled retail service in the first instance. If FERC does not have such jurisdiction under the Federal Power Act, it is irrelevant whether, as a policy matter, FERC's failure to impose a remedy is adversely affecting Enron's interests as an unbundled transmission user in other markets. FERC's jurisdiction under FPA § 206 to eliminate undue discrimination applies to the facilities and services over which it has jurisdiction. It does not give the FERC unbridled authority to regulate services that are subject to exclusive State jurisdiction.

Second, FERC's findings of undue discrimination in Order No. 888 involved the potential for transmission-owning utilities to favor their own power sales in markets where the utilities must compete for those sales. FERC did not make factual findings in Order No. 888 that transmission-owning utilities engaged in undue discrimination against competitors with respect to the utilities' bundled retail sales, because there is no competition for such sales. A utility providing service to bundled retail customers generally has an exclusive state franchise to serve those customers, and a comparable finding of undue discrimination with respect to that endeavor is not even an abstract possibility.

Third, Enron focuses on a different issue—whether utilities in states adhering to the traditional model of bundled service have discriminated unduly in favor of transmissions to their

native load and against transmissions to customers receiving unbundled service in competitive power markets in other states. However, FERC did not make any specific findings of undue discrimination on this issue, and Enron did not appeal FERC's failure to make such findings.

In order for FERC to find that such discrimination exists under the Federal Power Act, it would first have to explore whether bundled retail customers are similarly situated to unbundled transmission customers, and whether any service differences are justified by the differences in customer characteristics.[41] FERC has previously recognized, and the reviewing court agreed, that bundled retail customers are *not* similarly situated with wholesale and unbundled retail customers. *See Northeast Utils. Serv. Co.*, 59 F.E.R.C. (CCH) ¶ 61,042, at 61,160 (1992), *aff'd*, 993 F.2d 937 (1st Cir. 1993); *cf. Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 299 (1997).

Bundled retail customers differ from those receiving unbundled service by the very fact that the former have no choice in service-providers. *See Northern States Power Co. v. FERC*, 176 F.3d 1090, 1095 (8th Cir. 1999) (most wholesale customers may use alternative supplies purchased from other utilities, whereas "[t]he native/retail consumer . . . is unable to turn to alternative sources of supply."), *cert. denied*, 528 U.S. 1182 (2000). As the Court recognized in *Tracy*, states might have various reasons for choosing to protect the residential customers who have no effective means

---

[41] Undue discrimination under the Federal Power Act has long been defined as the disparate treatment of similarly situated FERC-jurisdictional customers. *E.g., Cities of Newark v. FERC*, 763 F.2d 533, 546 (3d Cir. 1985); *Metro. Edison Co. v. FERC*, 595 F.2d 851, 857 (D.C. Cir. 1979); *Pub. Serv. Co. of Ind., Inc. v. FERC*, 575 F.2d 1204, 1212 (7th Cir. 1978); *St. Michaels Utils. Comm'n v. FPC*, 377 F.2d 912, 916 (4th Cir. 1967). These precedents recognize that differences in customer characteristics may justify the imposition of different regulatory rules.

of choosing an alternative supplier. *See Gen. Motors Corp. v. Tracy*, 519 U.S. at 304-06. Indeed, traditional bundled service involves a "regulatory bargain," wherein the utility receives an exclusive franchise but assumes certain duties to its customers. "In return for this obligation to serve, the native load customers regularly bear the cost of transmission facilities; native load customers pay for them, use them, plan on them, and rely on them." *Northeast Utils. Serv. Co. v. FERC*, 993 F.2d 937, 954 (1st Cir. 1993); *see also* Order No. 888-A, 62 Fed. Reg. at 12,301. Thus, FERC has held that it is not discrimination when a utility providing service to its native load customers reserves transmission capacity for that purpose, and that view has been affirmed. *Id.*

The FERC also took concrete steps within the scope of its jurisdiction to address the concern of Enron and its allies that utilities will abuse their right to reserve transmission for their native load. FERC has consistently made clear that it will review a utility's available transmission capacity calculations, including the "set-aside" for bundled retail service (*i.e.*, for "native load"), to ensure that utilities do not arbitrarily withhold transmission capacity from the open access market. Thus, in several post-Order No. 888 cases, the FERC has reviewed utilities' transmission reservations for bundled retail load, and in some cases has ordered utilities to release capacity for use under open access tariffs.[42] FERC has also taken other steps to ensure that its supervision over reservations of capacity for the native load provides an

---

[42] *E.g., Wisconsin Power & Light Co.*, 84 F.E.R.C. (CCH) ¶ 61,120, at 61,658-59 (1998); *El Paso Elec. Co.*, 87 F.E.R.C. (CCH) ¶ 61,202 (1999); *Arizona Pub. Serv. Co. v. Idaho Power Co.*, 87 F.E.R.C. (CCH) ¶ 61,303, at 62,223 (1999); *see also Capacity Benefit Margin in Computing Available Transmission Capacity*, Order Clarifying Methodology for Computing Available Transmission Capability, 88 F.E.R.C. (CCH) ¶ 61,099 (1999).

effective remedy.[43] And with respect to any capacity that is available for open access transmission, customers under the Order No. 888 open access tariff must receive the same degree of firmness as the utility's native load.[44] FERC has not left a jurisdictional void that utilities are able to use to unfairly restrict transactions in competitive markets.[45]

Lastly, Enron's brief seems to suggest that FERC should have exercised jurisdiction over bundled retail sales in order to facilitate retail competition in those States that have not volunteered to endorse this change. Enron Br. 34-38. Thus, it appears Enron may be using this jurisdictional dispute to help open up those retail markets for competition in order to obtain a broader customer base for its competitive services. As noted earlier, Congress has spoken to this question. Section 212(h) leaves to the States the question whether to require utilities to provide unbundled transmission services for retail customers. In the proper exercise of jurisdiction over matters of local concern, States may legitimately conclude that retail services should not be supplied competitively, and thus maintain their jurisdiction over all aspects of such services. It is this very choice that FERC correctly left to the States.

---

[43] For example, FERC ruled that public utilities must identify their sources of generated or purchased power in order to permit other parties to ascertain whether the utilities' transmission set asides for bundled retail customers are reasonable. Order No. 888, 61 Fed. Reg. at 21,605.

[44] *Id.*

[45] Enron's amici raise various policy arguments about abusive or sham reservations for native load transmissions. These arguments belong before FERC or state commissions, not before the Court. Their concerns can and should be addressed through government policy. For example, a key objective of the Administration's recently announced energy plan is to expand transmission capacity to eliminate constraints on the grid. *See* Report of the National Energy Policy Development Group, "Reliable, Affordable, and Environmentally Sound Energy for America's Future," available at *www.whitehouse.gov/energy/ Overview*.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted,

EDWARD H. COMER
BARBARA A. HINDIN
EDISON ELECTRIC INSTITUTE
701 Pennsylvania Ave., N.W.
Washington, D.C. 20004
(202) 508-5000

CHARLES G. COLE
Counsel of Record
DAVID B. RASKIN
ALICE E. LOUGHRAN
STEPTOE & JOHNSON LLP
1330 Connecticut Ave., N.W.
Washington, D.C. 20036
(202) 429-6270

Counsel for Respondent Edison Electric Institute

APPENDIX

APPENDIX

Section 201 of the Federal Power Act, 16 U.S.C. § 824 provides in relevant part:

Declaration of policy; application of subchapter

(a) Federal regulation of transmission and sale of electric energy

It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III of this chapter and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce

(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy or over facilities used in local distribution or only for the

transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

(2) The provisions of sections 824i, 824j, and 824k of this title shall apply to the entities described in such provisions, and such entities shall be subject to the jurisdiction of the Commission for purposes of carrying out such provisions and for purposes of applying the enforcement authorities of this chapter with respect to such provisions. Compliance with any order of the Commission under the provisions of section 824i or 824j of this title, shall not make an electric utility or other entity subject to the jurisdiction of the Commission for any purposes other than the purposes specified in the preceding sentence.

(c) Electric energy in interstate commerce

For the purpose of this subchapter, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale" defined

The term "sale of electric energy at wholesale" when used in this subchapter, means a sale of electric energy to any person for resale.

Section 212(h) of the Federal Power Act, 16 U.S.C. § 824k(h), provides:

(h) Prohibition on mandatory retail wheeling and sham wholesale transactions

No order issued under this chapter shall be conditioned upon or require the transmission of electric energy:

(1) directly to an ultimate consumer, or

(2) to, or for the benefit of, an entity if such electric energy would be sold by such entity directly to an ultimate consumer, unless:

(A) such entity is a Federal power marketing agency; the Tennessee Valley Authority; a State or any political subdivision of a State (or an agency, authority, or instrumentality of a State or a political subdivision); a corporation or association that has ever received a loan for the purposes of providing electric service from the Administrator of the Rural Electrification Administration under the Rural Electrification Act of 1936 [7 U.S.C. § 901 *et seq.*]; a person having an obligation arising under State or local law (exclusive of an obligation arising solely from a contract entered into by such person) to provide electric service to the public; or any corporation or association which is wholly owned, directly or indirectly, by any one or more of the foregoing; and

(B) such entity was providing electric service to such ultimate consumer on October 24, 1992, or would utilize transmission or distribution facilities that it owns or controls to deliver all such electric energy to such electric consumer.

Nothing in this subsection shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an ultimate consumer.

Section 313(b) of the Federal Power Act, 16 U.S.C. § 825*l*(b), reads in pertinent part:

(b) Judicial review

Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the United States Court of Appeals . . . Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the

Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of title 28.

Sections 1(a) and (b) of the Natural Gas Act, 15 U.S.C. §§ 717(a), (b), provide:

Regulation of natural gas companies

(a) Necessity of regulation in public interest

As disclosed in reports of the Federal Trade Commission made pursuant to S.Res. 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest.

(b) Transactions to which provisions of chapter applicable

The provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

Section 7(c) of the Natural Gas Act, 15 U.S.C. § 717f(c), reads:

(c) Certificate of public convenience and necessity

(1)(A) No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: Provided, however, That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on February 7, 1942, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after February 7, 1942. Pending the determination of any such application, the continuance of such operation shall be lawful.

(B) In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: Provided, however, That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to

serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest.

(2) The Commission may issue a certificate of public convenience and necessity to a natural-gas company for the transportation in interstate commerce of natural gas used by any person for one or more high-priority uses, as defined, by rule, by the Commission, in the case of—

(A) natural gas sold by the producer to such person; and

(B) natural gas produced by such person.

18 C.F.R. § 35.28, reads in relevant part:

Non-discriminatory open access transmission tariff.

(a) Applicability. This section applies to any public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce and to any non-public utility that seeks voluntary compliance with jurisdictional transmission tariff reciprocity conditions.

* * * *

(c) Non-discriminatory open access transmission tariffs.

(1) Every public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce must have on file with the Commission a tariff of general applicability for transmission services, including ancillary services, over such facilities. Such tariff must be the open access pro forma tariff contained in Order No. 888, FERC Stats. & Regs. ¶ 31,036 (Final Rule on Open Access and Stranded Costs) or

such other open access tariff as may be approved by the Commission consistent with Order No. 888, FERC Stats. & Regs. ¶ 31,036.

* * * *

(2) Every public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce, and that uses those facilities to engage in wholesale sales and/or purchases of electric energy, or unbundled retail sales of electric energy, must take transmission service for such sales and/or purchases under the open access tariff filed pursuant to this section.

MAY 31 2001

No. 00-568

IN THE
Supreme Court of the United States
OCTOBER TERM, 2001

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, ET AL.,

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF THE TRANSMISSION ACCESS POLICY STUDY GROUP AS RESPONDENT IN NO. 00-568

ROBERT C. MCDIARMID
COUNSEL OF RECORD
CYNTHIA S. BOGORAD
PETER J. HOPKINS
Spiegel & McDiarmid
Suite 1000
1350 New York Ave., NW
Washington, DC 20005

BEST AVAILABLE COPY

QUESTION PRESENTED IN NO. 00-568

By Order filed February 26, 2001, this Court granted certiorari with respect to the following question:

> Whether, given that Congress in 1935 stated that federal regulation extends "only to those matters which are not subject to regulation by the States" (Federal Power Act (FPA) § 201(a), 16 U.S.C. § 824(a)), and the transmission of energy from generators to retail customers in the same state was then "subject to regulation by the states" (as it has been since 1935), may the Federal Energy Regulatory Commission (FERC) preempt state jurisdiction over such intrastate retail transmission of electric energy?

RULE 29.6 STATEMENT

The Transmission Access Policy Study Group ("TAPS") is an informal association of transmission dependent utilities in more than twenty-five states, promoting open and non-discriminatory transmission access. While most TAPS members are municipal utilities, or associations or agencies thereof, one, Madison Gas & Electric Company ("MGE"), is a publicly held investor-owned utility. MGE has no parent company and no publicly held company owns 10% or more of MGE's stock.

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED i
RULE 29.6 STATEMENT ii
TABLE OF AUTHORITIES v
STATEMENT 1
- A. Interest of TAPS 3
- B. Evolution of the Electric Industry 4
- C. Retail Competition 7
- D. Orders Below 11

SUMMARY OF ARGUMENT 14
ARGUMENT 16
I. THE STATES' ANALYSIS DOES NOT COMPORT WITH THE PLAIN LANGUAGE OF THE STATUTE 16
- A. Section 201(b)(1) Grants FERC Jurisdiction Over All Transmission of Electric Energy In Interstate Commerce, Not "Wholesale Sales and Associated Transmission In Interstate Commerce" 17
- B. The General Policy Declaration of Section 201(a) Cannot Undermine The Specific Grant of Jurisdiction To FERC Under Section 201(b)(1) 20
- C. The Plain Language Distinguishes Between Interstate Transmission and Local Distribution 21
- D. The Language of Section 206(d) Does Not Support the States' Position 24
- E. Sections 211 and 212 Do Not Support The States' Position 26

II. FERC CORRECTLY FOUND THAT ALL TRANSMISSION ON THE INTERCONNECTED GRID IS IN INTERSTATE COMMERCE 27
III. ONLY FERC IS COMPETENT TO REGULATE INTERSTATE TRANSMISSION 31
IV. FERC'S ASSERTION OF JURISDICTION DID NOT INVADE EXCLUSIVE STATE DOMAIN 38
- A. FERC Has Regulated Unbundled Retail Transmission For Decades 38
- B. FERC Cannot Be Faulted For Responding Promptly To The New Market Development Of Retail Electric Competition 41
- C. The States' Policy Arguments Cannot Eliminate the Need for Federal Regulation of the Interstate Transmission Required for Retail Choice Programs 43

CONCLUSION 45

TABLE OF AUTHORITIES

CASES

Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) 23
Arkansas Power & Light Co. v. FPC, 368 F.2d 376 (8th Cir. 1966) 28, 29
Bates v. United States, 522 U.S. 23 (1997) 18, 22
Buck v. Kuykendall, 267 U.S. 307 (1925) 36
In re California Power Exchange Corp., 245 F.3d 1110 (9th Cir. 2001) 2, 10
Connecticut Light & Power Co v. FPC, 324 U.S. 515 (1945) 20, 22
FPC v. Florida Power & Light Co., 404 U.S. 453 (1972) 28
FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) 23, 31, 36, 37
FPC v. Southern California Edison Co., 376 U.S. 205 (1964) 20, 42
Gibbons v. Ogden, 22 U.S. 1 (1824) 37
Gulf States Utilities Co. v. FPC, 411 U.S. 747 (1973) 5, 38
Healy v. The Beer Institute, 491 U.S. 324 (1989) 32
Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953 (1986) 25
New England Power Co. v. New Hampshire, 455 U.S. 331 (1982) 28, 37
Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) 5
Public Utilities Commission of California v. FERC, 143 F.3d 610 (D.C. Cir. 1998) 24
Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir. 2000) 13
United States v. Ron Pair Enterprises, Inc., 489 U.S. 235 (1989) 17

STATUTES

A.B. 6 § 3, 2001 Leg., 1st Ex. Sess. (Cal. 2001) 36
A.B. 1890, 1996 Leg., Reg. Sess. (Cal. 1996) 41
A.B. 1890 § 1(c), 1996 Leg., Reg. Sess. (Cal. 1996) 10
Energy Policy Act of 1992, Pub. L. No. 95-617, 92 Stat. 3117 (1978) 6
Federal Power Act,
16 U.S.C. § 824(a) 16, 19, 20, 24
16 U.S.C. § 824(b) 14, 20, 21
16 U.S.C. § 824(b)(1) ..... *passim*
16 U.S.C. § 824(c) 19, 20
16 U.S.C. § 824d 5
16 U.S.C. § 824e 5
16 U.S.C. § 824e(a) 25
16 U.S.C. § 824e(d) 24, 25
16 U.S.C. § 824j 6
16 U.S.C. § 824k 6
16 U.S.C. § 824k(a) 26
16 U.S.C. § 824k(e) 26
16 U.S.C. § 824k(h) 12, 26, 27
Illinois Electric Service Customer Choice and Rate Relief Law of 1997, 220 Ill. Comp. Stat. 5/16-101A(b), (d) (1997) 8
220 Ill. Comp. Stat. 5/16-126(a) (1997) 10
Massachusetts Electric Restructuring Act of 1997, Mass. Gen. Laws ch. 164, § 1(c) (1997) 8, 10
Montana Electric Utility Industry Restructuring and Customer Choice Act of 1997, Mont. Code Ann. §§ 69-8-102(1), (2) (1997) 8
N.J. Stat. Ann. § 48:3-78 (1999) 10

Natural Gas Act,
15 U.S.C. § 717(b) 23
15 U.S.C. § 717(c) 24
Oklahoma Electric Restructuring Act of 1997, Okla. Stat. tit. 17, § 190.2 (1997) 8
Pennsylvania Electric Generation Customer Choice and Competition Act of 2000, 66 Pa. Cons. Stat. §§ 2802(13), (14) (2000) 8
66 Pa. Cons. Stat. § 2809 (2000) 9
Public Utility Regulatory Policies Act of 1978, Pub. L. No. 102-486, 106 Stat. 2921 (1992) 6
Virginia Electric Utility Restructuring Act of 1999,
Va. Code Ann. § 56.577 (1999) 10
Va. Code Ann. § 56.585(B)(2) (2001) 9
Va. Code Ann. § 56.587(B) (1999) 9

ADMINISTRATIVE CASES & MATERIALS

American Electric Power Service Corp., 67 F.E.R.C. ¶ 61,168, *clarified*, 67 F.E.R.C. ¶ 61,317 (1994) 7
Consolidated Edison Co. of New York, Inc., 15 F.E.R.C. ¶ 61,173 (1981) 39
Consumers Power Co. (Midland Plant, Units 1 & 2), 6 N.R.C. 892 (1977) 5
Florida Power & Light Co., 27 F.E.R.C. ¶ 61,333 (1984) 29
Florida Power & Light Co., 37 F.P.C. 544 (1967), *aff'd sub nom. FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972) 29

In the Matter of Hartford Electric Light Co., 2 F.P.C. 502 (1941), *aff'd sub nom. Hartford Electric Light Co.*, 131 F.2d 953 (2d Cir. 1942) 23
Heartland Energy Service, Inc., 68 F.E.R.C. ¶ 61,223 (1994) 7
Illinois Power Co., 95 F.E.R.C. ¶ 61,183, 2001 FERC LEXIS 1018 (May 8, 2001) 44
Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement, Order No. 592, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,044, 61 Fed. Reg. 68595 (Dec. 30, 1996), *recons. denied*, Order No. 592-A, 79 F.E.R.C. ¶ 61,321 (1997) 6
Niagara Mohawk Power Corp., 34 F.E.R.C. ¶ 61,028 (1986) 39
Niagara Mohawk Power Corp., 51 F.E.R.C. ¶ 61,273 (1990) 40
Niagara Mohawk Power Corp., 82 F.E.R.C. ¶ 63,018 (1998), *aff'd in relevant part*, 92 F.E.R.C. ¶ 61,168 (2000) 40
Pacific Gas & Electric Co., 20 F.E.R.C. ¶ 61,190, *order on reh'g and clarification*, 21 F.E.R.C. ¶ 61,115 (1982) 40
Pacific Gas & Electric Co., 50 F.E.R.C. ¶ 61,383 (1990) 40
Pacific Gas & Electric Co., 56 F.E.R.C. ¶ 61,322 (1991) 40
Pacific Gas & Electric Co., 77 F.E.R.C. ¶ 61,204 (1996), *reh'g denied*, 81 F.E.R.C. ¶ 61,122 (1997) 10
Power Authority of New York v. Niagara Mohawk Power Corp., 79 F.E.R.C. ¶ 61,159 (1997) 39

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, [1991-1996 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (May 10, 1996) ..... *passim*

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-A, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (Mar. 14, 1997) 11, 41

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,662 (Apr. 7, 1995) 5, 11

Public Service Co. of Colorado, 62 F.E.R.C. ¶ 61,013 (1993) 28

Public Service Co. of Indiana, Inc., 51 F.E.R.C. ¶ 61,367 (1990), *order on clarification*, 53 F.E.R.C. ¶ 61,131 (1990), *petition for review dismissed sub nom. North Indiana Public Service Co. v. FERC*, 954 F.2d 736 (D.C. Cir. 1992) 7

Regional Transmission Organizations, Order No.2000, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,089, 65 Fed. Reg. at 810 (Jan. 6, 2000), *order on reh'g*, Order 2000-A, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,092, 65 Fed. Reg. 12,088 (Mar. 8, 2000), *appeal docketed sub nom. Pub. Util. Dist. 1 v. FERC*, No. 00-1174 (D.C. Cir. Apr. 24, 2000) 44

San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services into Markets Operated by the California Independent System Operator and the California Power Exchange, 93 F.E.R.C. ¶ 61,121, *order directing remedies*, 93 F.E.R.C. ¶ 61,294 (2000), *reh'g pending* 9

Wisconsin Electric Power Co., 46 F.E.R.C. ¶ 61,019, *reh'g denied*, 48 F.E.R.C. ¶ 61,247 (1989), *petition for review denied per curiam sub nom. Wisconsin Public Power Inc. System v. FERC*, 918 F.2d 225 (D.C. Cir. 1990) 6

ARTICLES

CNN, *Sagging power lines, hot weather blamed for blackouts*, CNN Interactive, Aug. 11, 1996, *at* http://www.cnn.com/US/9608/11/power.outage. 30

Kamp, Jon, *Wholesale Power Mkt May Sour Dereg In Illinois – Report*, Wall St. J., May 9, 2001, *available at* http://interactive.wsj.com/archive/retrieve.cgi?id=DI-CO-20010509-003071.djm. 9

OTHER AUTHORITIES

Commerce Clause, U.S. Const. art. I, § 8 cl. 3 37
Federal Power Commission, Vol. 1 – Report of the Commission, Prevention of Power Failures (July 1967) 30
Governor Gray Davis, State of the State Address (Jan. 8, 2001), *text available at* http://www.governor.ca.gov/state/govsite/gov_homepage.jsp. 37

No. 00-568

IN THE
Supreme Court of the United States
OCTOBER TERM, 2001

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, ET AL.,

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF THE TRANSMISSION ACCESS POLICY STUDY GROUP AS RESPONDENT IN NO. 00-568

STATEMENT OF THE CASE

Petitioners State of New York, *et al.* ("New York") challenge the Federal Energy Regulatory Commission's ("FERC" or "Commission")[1] assertion of jurisdiction over the rates, terms, and conditions of interstate transmission service by public utilities where states have elected to depart radically from traditional regulation of retail electricity sales. The issue raised by New York is limited to states that have adopted "retail competition," a regimen where a retail consumer may purchase electricity from the electricity supplier it chooses and have that energy "wheeled" over the interstate transmission facilities of its former monopoly supplier and others. New York objects to FERC's determination that such unbundled transmission service is within its jurisdiction under the Federal Power Act ("FPA"),

[1] As used herein, "FERC" or "Commission" also includes FERC's predecessor, the Federal Power Commission, where applicable.

and is subject to the uniform tariffs that apply to wholesale use of the same interstate transmission facilities.

New York attempts to cast a state's implementation of retail competition as business as usual, calling it merely "a change in bill format." (NY Br. at 8.) It claims that unbundling "does not necessarily alter the total due on a customer's bill" and is just "an accounting mechanism that allows customers the option of obtaining one or more retail service elements from competitive providers." (*Id.* at 9.)

Unbundling, or breaking out, the transmission supporting retail electricity sales is an element essential to state retail choice or retail competition programs. The terms "deregulation" and "restructuring" are commonly used to describe such state initiatives, which effect a profound change in the way electricity is purchased, sold, and regulated.[2] While the specifics of the retail choice regimes adopted by the various states differ, their fundamental premise is the same: replacement of state cost-of-service regulation of the generation function of a vertically integrated monopolist with direct retail customer access, via the interstate transmission facilities of their former supplier and others, to competitive generation markets.

Relying on the Federal Power Act's broad grant of jurisdiction over "the transmission of electric energy in interstate commerce" in Section 201(b)(1), 16 U.S.C. § 824(b)(1), FERC asserted jurisdiction over unbundled transmission for retail customers in the orders on review and extended its remedy for undue discrimination to this use of interstate transmission.[3] FERC placed unbundled

[2] *See, e.g., In re California Power Exchange Corp.*, 245 F.3d 1110, 1114 (9th Cir. 2001) (describing the "major restructuring" embarked on by the California legislature).

[3] *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, [1991-1996 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (May 10, 1996), *clarified*, 76 F.E.R.C. ¶ 61,009 (1996), *modified*, Order No. 888-A, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (Mar. 14, 1997), *order on reh'g*, Order No. 888-B, 81 F.E.R.C. ¶ 61,248, 62 Fed. Reg. 64,688 (Dec. 9, 1997), *aff'd in part and remanded in part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *petitions for cert. granted sub nom. New York v. FERC*, No. 00-568 and *Enron Power Marketing, Inc. v. FERC*, No. 00-809 (U.S. Feb. 26, 2001), *order on reh'g*, Order No. 888-C, 82 F.E.R.C. ¶ 61,046 (1998).

transmission for retail choice customers under the open access transmission tariffs it required for wholesale users, providing such retail customers access to the interstate transmission grid (which they must share with other users) on the non-discriminatory terms FERC found essential for competitive electricity markets to develop and thrive.[4] In this way, FERC established the regulatory underpinning necessary to support a state's decision to permit retail customers direct access to competitive interstate markets.

A. Interest of TAPS

The Transmission Access Policy Study Group ("TAPS") is an informal association of transmission dependent utilities in more than twenty-five states, promoting open and non-discriminatory transmission access. To serve their customers reliably and at reasonable cost, TAPS members rely (in whole or in part) on wholesale power purchases and energy from their own remote resources. As a result, TAPS members must depend on the transmission facilities owned and controlled by others. This dependence has placed TAPS

[4] The transmission service that public utilities provide themselves for purposes of making bundled retail sales is also transmission in interstate commerce. Particularly in the context of competitive electricity markets, differences between the bundled transmission service that utilities provide themselves and the transmission provided to their competitors raise issues of undue discrimination that are before the Court in No. 00-809. TAPS supports Petitioner Enron's position in No. 00-809, but limits itself to responding to New York's (and *amicus* California's) challenge to FERC's jurisdiction in this docket.

members on the front line of battles for equal transmission access. They have experienced first-hand the competitive disadvantage and market disruption that results from discriminatory limits on access to interstate transmission.[5]

B. Evolution of the Electric Industry

Traditionally, the electric industry was largely comprised of vertically integrated, investor-owned electric utilities that operated as regulated monopolies. They would own the generation, transmission, and distribution facilities required to serve, on a bundled (combined delivered product) basis, retail customers within their franchised service areas and embedded wholesale customers (municipal, cooperative or smaller investor-owned utilities located on their transmission system).[6] Each utility's transmission system was largely used to integrate its own generation to serve its retail and wholesale customers. With weak interconnections and the inefficiencies then inherent in long distance transmission, there was limited coordination among utilities, and little unbundled transmission service.[7]

Starting in the late 1960s, with rising power costs and increasing efficiency of long distance transmission, wholesale customers sought access to sources other than their surrounding bundled supplier.[8] Because wholesale customers were typically transmission dependent islands in the sea of their existing supplier, a purchase from another utility (or participation in an efficient generating unit) required transmission service from their existing supplier.

---

[5] Many of the examples of discriminatory transmission cited in Order 888 pertain to TAPS members. *See* Order 888, 61 Fed. Reg. at 21,567-69, 21,702-06, Enron App. D at 213a-21[illegible]a, 315a-331a. Citations in this brief to "Enron App." are to the Appendix filed with Enron's Petition for Writ of Certiorari in No. 00-809.

[6] *See* Order 888, 61 Fed. Reg. at 21,543, Enron App. D at 141a.

[7] *See id.*

[8] *See* Order 888, 61 Fed. Reg. at 21,544-45, Enron App. D at 146a-147a.

Transmission dependent utilities often were able to negotiate some form of "voluntary" transmission service, albeit sometimes with the help of antitrust license conditions imposed by the Nuclear Regulatory Commission[9] or the threat of antitrust litigation.[10] However, this transmission service was typically inferior to the service that the vertically-integrated transmission owner provided itself.[11] Although the Federal Power Act expressly required the Commission to ensure that the rates, terms, and conditions of transmission service were just and reasonable and not unduly discriminatory or preferential,[12] and notwithstanding this Court's instruction that the FPA "clearly carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of the interstate utility operations pursuant to §§ 202 and 203, and under like directives in §§ 205, 206, and 207,"[13] the Commission was reluctant to test its authority to require more transmission service than a utility voluntarily offered.[14] Instead, FERC generally limited itself to determining transmission rates for unbundled transmission contracts or the transmission component of bundled wholesale sales. When discrimination issues were raised, FERC measured undue discrimination

---

[9] *See, e.g., Consumers Power Co.* (Midland Plant, Units 1 & 2), 6 N.R.C. 892, 1043 (1977).

[10] *See Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973). *See generally* Order 888, 61 Fed. Reg. at 21,546 & n.51, Enron App. D at 152a-153a.

[11] *See Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Notice of Proposed Rule Making and Supplemental Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,662, 17,676 (Apr. 7, 1995) ("NOPR"), Enron App. F at 610a-620a; Order 888, 61 Fed. Reg. at 21,567-69, 21,703-06, Enron App. D at 213a-218a, 315a-331a.

[12] Sections 205 and 206, 16 U.S.C. §§ 824d and 824e.

[13] *Gulf States Utils. Co. v. FPC*, 411 U.S. 747, 758-59 (1973).

[14] *See* Order 888, 61 Fed. Reg. at 21,561-62, Enron App. D at 184a-189a.

only as between similarly situated wholesale customers, ignoring the superior terms implicit in the service the vertically integrated transmission owner provided itself.[15]

Through the 1978 Public Utility Regulatory Policies Act ("PURPA")[16] and particularly with the enactment of the 1992 Energy Policy Act ("EPAct"),[17] new classes of competitive wholesale generators emerged, which depended on transmission provided by others to market their output.[18] FERC's PURPA-initiated authority to order wholesale transmission service pursuant to FPA Sections 211 and 212, 16 U.S.C. §§ 824j, 824k, was expanded and strengthened by EPAct. FERC found that EPAct evinced Congressional intent that the Commission promote competitive electricity markets, and a recognition of the role of transmission as the essential highways for this interstate commerce.[19]

On the premise that in the absence of market power the competitive market could be depended upon to discipline prices to the statutory just and reasonable level, FERC began authorizing "market-based rates" at wholesale where a particular seller had demonstrated that it (and its affiliates) did not possess or had mitigated market power in generation and transmission. Vertically integrated utilities could show

[15] *See, e.g., Wisconsin Elec. Power Co.*, 46 F.E.R.C. ¶ 61,019, at 61,113-16, *reh'g denied*, 48 F.E.R.C. ¶ 61,247, at 61,861-62 (1989), *petition for review denied per curiam sub nom. Wisconsin Public Power Inc. System v. FERC*, 918 F.2d 225 (D.C. Cir. 1990).

[16] Pub. L. No. 95-617, 92 Stat. 3117 (1978) (codified in U.S.C. titles 15, 16, 26, 40, 42, and 43).

[17] Pub. L. No. 102-486, 106 Stat. 2921 (1992) (codified at, among other places, 15 U.S.C. § 79a-51 and 16 U.S.C. §§ 796 (22-25), 824j-l).

[18] *See* Order 888, 61 Fed. Reg. at 21,545, Enron App. D at 147a-156a.

[19] *See* Order 888, 61 Fed. Reg. at 21,562-63, Enron App. D at 191a-193a. *See also Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,044, 61 Fed. Reg. 68,595, 68,596 (Dec. 30, 1996), *recons. denied*, Order No. 592-A, 79 F.E.R.C. ¶ 61,321 (1997).

mitigation of transmission market power by offering an "open access" tariff.[20] In this context, the Commission first began to consider the service the vertically integrated transmission owner provided itself as the benchmark for undue discrimination.[21]

In 1994, in light of changing industry conditions and increasing competition, the Commission reevaluated its standards for undue discrimination. The Commission broadened the focus of undue discrimination to include consideration of the transmission owner's own use of its transmission system. To be found not unduly discriminatory, an open access tariff would have to offer third parties access "under the same or comparable terms and conditions ... as the transmission provider's uses of its system."[22]

C. Retail Competition

Against the backdrop of growing wholesale competition an ever louder drumbeat for retail choice began to be heard, especially in higher cost states, to enable retail customers to enjoy the anticipated savings from competitive electricity markets.[23] Currently, some 25 states have through their legislatures or regulatory commissions taken some steps to

[20] *See, e.g., Heartland Energy Serv., Inc.*, 68 F.E.R.C. ¶ 61,223, at 62,060 (1994). *See also* Order 888, 61 Fed. Reg. at 21,553.

[21] *See, e.g., Public Serv. Co. of Indiana, Inc.*, 51 F.E.R.C. ¶ 61,367, at 62,201 (to prevent "unfair competitive advantage" in marketing bulk power, PSI must serve itself under the terms of the same transmission tariff to which other utilities are subject), *reh'g denied*, 52 F.E.R.C. ¶ 61,260, *order on clarification*, 53 F.E.R.C. ¶ 61,131 (1990), *petition for review dismissed sub nom. North Indiana Public Serv. Co. v. FERC*, 954 F.2d 736 (D.C. Cir. 1992).

[22] *American Elec. Power Serv. Corp.*, 67 F.E.R.C. ¶ 61,168, at 61,490, *clarified*, 67 F.E.R.C. ¶ 61,317 (1994), discussed in Order 888, 61 Fed. Reg. at 21,547-48, Enron App. D at 159a-162a.

[23] *See* Order 888, 61 Fed. Reg. at 21,550 & n.101, Enron App. D at 431a & n.101-432a; Order 888-A, 62 Fed. Reg. at 12,280-81, Enron App. E at 402a-403a.

adopt retail competition.[24] In states implementing retail choice, the contractual and regulatory paradigm, and the resulting use of the transmission system, depart starkly from the traditional regulatory regimen described by New York. (NY at Br. 4-6.)

The specifics of state retail choice programs vary widely, but they share a common element: use of the interstate transmission grid "to allow direct access by retail consumers to the competitive market for the generation of electricity."[25] States adopting retail competition have decided that the public would be "best served by moving from (i) the regulatory framework ... in which retail electricity service is provided principally by public utility corporations obligated to provide ultimate consumers in exclusive service territories with reliable electric service at regulated rates, to (ii) a framework under which competitive producers will supply electric power and customers will gain the right to choose their electric power supplier."[26] Retail customers are invited

[24] (*See* NY Br. at 9 n.5.)

[25] Oklahoma Electric Restructuring Act of 1997, Okla. Stat. tit. 17, § 190.2 (1997), Section 2. *See also* Montana Electric Utility Industry Restructuring and Customer Choice Act of 1997, Mont. Code Ann. §§ 69-8-102(1), (2) (1997) ("(1) The generation and sale of electricity is becoming a competitive industry. (2) Montana customers should have the freedom to choose their supplier of electricity and related services in a competitive market...").

[26] Massachusetts Electric Restructuring Act of 1997, Mass. Gen. Laws ch. 164, § 1(c) (1997). *See also* Pennsylvania Electric Generation Customer Choice and Competition Act, 66 Pa. Cons. Stat. §§ 2802(13), (14) (2000) (provides for "transition from the current regulated structure to a structure under which retail customers will have direct access to a competitive market for the generation and sale or purchase of electricity" and "requires electric utilities to unbundle their rates and services and to provide open access over their transmission and distribution systems to allow competitive suppliers to generate and sell electricity directly to consumers in this Commonwealth"); Illinois Electric Service Customer Choice and Rate Relief Law of 1997, 220 Ill. Comp. Stat. 5/16-101A(b), (d) (1997) ("Long-standing regulatory relationships need to be altered to

to deal directly with competitive generation suppliers,[27] and to have their energy purchase "wheeled" over the interstate grid, including the transmission facilities of their former monopoly supplier.[28] This direct access to competitive generation markets substitutes for regulation and is expected to provide consumers efficient, low cost, and reliable power.

The success of retail deregulation is inextricably tied to the effectiveness of interstate wholesale markets on which such regimens necessarily depend.[29] Some states established new market structures to facilitate competition. For example, in what California refers to as its "now notorious electric utility deregulation experiment" (CA Br. at 1), investor-owned utilities initially were required to sell the output of their generation to a state-established power exchange, and then buy on the wholesale spot market the energy required to meet

accommodate the competition that could fundamentally alter the structure of the electric services market").

[27] Such competitive suppliers include independent generators, regional or national marketers (like Enron), and other utilities. Some states license suppliers to ensure, *e.g.*, financial responsibility. *See, e.g.*, Virginia Electric Restructuring Act of 1999, Va. Code Ann. § 56-587(B) (1999); 66 Pa. Cons. Stat. § 2809 (2000).

[28] The former supplier may take on a new role as "default supplier" for customers that do not choose a competitive supplier (or where the competitive supplier fails to perform), although some state laws authorize assignment of the default supplier function by competitive bidding. *See, e.g.*, Va. Code Ann. § 56-585(B)(2) (2001).

[29] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Services into Markets Operated by the California Independent System Operator and the California Power Exchange*, 93 F.E.R.C. ¶ 61,121, at 61,350 ("a well functioning competitive wholesale power market in California, which includes a well functioning regional transmission grid, is a fundamental part of the solution to the supply problems and price volatility in California"), *order directing remedies*, 93 F.E.R.C. ¶ 61,294 (2000), *reh'g pending. See also*, Jon Kamp, *Wholesale Power Mkt May Sour Dereg In Illinois - Report*, Wall St. J., May 9, 2001, *available at* http://interactive.wsj.com/archive/retrieve.cgi?id=DI-CO-20010509-003071.dim.

the needs of customers located on their distributions systems that did not select a new supplier.[30] Before energy reached such a retail customer, it would go through multiple wholesale transactions as it was sold into and out of these centralized markets.[31]

Some state deregulation programs were developed against the background of "independent system operators" formed by power pools (at FERC encouragement[32]) to operate multi-utility transmission facilities on an efficient and non-discriminatory basis under a regional tariff.[33] Other states recognized the importance of region-wide transmission to broadening generation markets, and increasing their competitiveness, by including in their restructuring law the requirement that vertically integrated utilities join independent regional transmission organizations.[34]

---

[30] *See In re California Power Exchange Corp.*, 245 F.3d at 1114-15 (describing California's "must sell" and "must buy" provisions, their evolution, and associated institutions).

[31] *See Pacific Gas & Electric Co.*, 77 F.E.R.C. ¶ 61,204, at 61,794-95 (1996), *reh'g denied*, 81 F.E.R.C. ¶ 61,122 (1997).

[32] *See* Order 888, 61 Fed. Reg. at 21,593-94 & n.417; *see also id.* at 21,594-97.

[33] *See, e.g.*, 1997 Mass. Gen. Laws ch. 164 § 1(c) (authorizing Massachusetts regulators to "coordinate with the operator of the bulk power system in New England" and "monitor any independent systems operator serving the New England/New York area formed through federal statute or regulation"); N.J. Stat. Ann. § 48:3-78 (1999) (referencing PJM Interconnection, L.L.C. independent system operator).

[34] *See, e.g.*, 220 Ill. Comp. Stat. 5/16-126(a) (1997) ("establishment of one or more independent system operators or their functional equivalents is required to facilitate the development of an open and efficient marketplace for electric power and energy"; each utility is required to apply to FERC to establish or join such an organization); Va. Code Ann. § 56-577 (1999) (each incumbent utility is required to join or establish a regional transmission entity); A.B. 1890 § 1(c), 1996 Leg., Reg. Sess. (Cal. 1996) (enacted) (expressing legislative intent to create an independent system operator).

D. Orders Below

In Orders 888 and 888-A, the Commission exercised its responsibility under Sections 205 and 206 of the FPA to remedy the widespread undue discrimination it found in interstate transmission service.[35] FERC identified discrimination as the single greatest impediment to competitive power markets.[36]

The Commission found non-discriminatory open access to interstate transmission service necessary to remove impediments to, and to promote, competitive electricity markets, consistent with the pro-competitive purposes of the Federal Power Act and EPAct.[37] To eliminate the "patchwork" of systems using different access terms,[38] to ensure "that the integrity and reliability of our electricity infrastructure is maintained,"[39] and "to foster broad access across multiple systems under standardized terms and conditions,"[40] the Commission ordered all public utilities to file transmission tariffs conforming to the *pro forma* open access tariff included in its rule. FERC required public utilities to take transmission service for their own wholesale sales under that tariff and to rely on the same transmission

---

[35] *See* Order 888, 61 Fed. Reg. at 21,567, Enron App. D at 213a-218a.

[36] *See* Order 888, 61 Fed. Reg. at 21,550, Enron App. D at 171a-172a. *See also* NOPR, 60 Fed. Reg. at 17,664, 17,675-76.

[37] *See* Order 888, 61 Fed. Reg. at 21,541, 21,550, 21,568-69, Enron App. D at 131a-134a, 171a-172a, 218a; Order 888-A, 62 Fed. Reg. at 12,275-76, Enron App. E at 380a-383a. FERC concluded that radical changes in the industry required it to find unduly discriminatory practices it had previously tolerated and to address directly the terms on which transmission owners used their own transmission system. Order 888, 61 Fed. Reg. at 21,568-69, Enron App. D at 217a-218a.

[38] Order 888, 61 Fed. Reg. at 21,541, Enron App. D at 133a.

[39] *Id.*

[40] Order 888, 61 Fed. Reg. at 21,598, Enron App. D at 259a.

information for wholesale marketing that they make available to others.[41]

The Commission's *pro forma* tariff contains the "specific terms and conditions" for non-discriminatory open access, rather than mere general principles as some utilities had urged.[42] The tariff is intended to be comprehensive.[43] It includes detailed specifications of the rights and obligations associated with the various types of transmission service required to be provided.[44] These include the procedures for requesting, reserving, assigning, modifying, and scheduling transmission service; evaluating transmission requests; deciding among competing requests for service; expanding facilities to satisfy transmission requests; and allocating curtailments in the event of insufficient capacity.[45]

In Order 888, the Commission also asserted jurisdiction over public utilities' provision of unbundled transmission in interstate commerce associated with state retail competition programs. Consistent with Section 212(h) of the FPA, 16 U.S.C. § 824k(h), the Commission left to individual states the determination as to whether to allow their retail customers to participate directly in competitive interstate markets through retail wheeling. However, FERC determined

[41] Order 888, 61 Fed. Reg. at 21,541, Enron App. D at 133a; Order 888-A, 62 Fed. Reg. at 12,299, Enron App. E at 451a.

[42] Order 888, 61 Fed. Reg. at 21,598, Enron App. D at 259a.

[43] Certain variations were permitted to conform to regional practice. Order 888, 61 Fed. Reg. at 21,598, Enron App. D at 259a- 260a. Public utilities were permitted subsequently to "propose variations that are consistent with or superior to the terms and conditions" of the *pro forma* tariff, Order 888, 61 Fed. Reg. at 21,598 n.434, Enron App D at 259a n.434; *accord id.*, 61 Fed. Reg. at 21,619, Enron App. D at 279a-280a, but not to "litigate fundamental terms and conditions set forth in the Final Rule." *Id.*

[44] The Commission found non-price terms and conditions inseparable from pricing and cost recovery. *See* Order 888, 61 Fed. Reg. at 21,598, Enron App. D at 258a.

[45] *See* Order 888, *pro forma* tariff, 61 Fed. Reg. at 21,706-24.

that where a state elects to implement retail competition, the unbundled transmission necessary to support a retail customer's purchase from a competitive electricity supplier is a separate FERC-jurisdictional service that must be provided pursuant to the open access tariffs applicable to wholesale customers.[46]

In asserting jurisdiction over unbundled retail transmission, the Commission recognized that all transmission service in the interconnected grid is in interstate commerce,[47] and made clear its concern with preventing "balkanized" power markets. Where "consistent with the Commission's open access policies and comparability," FERC committed to defer to state requests to adapt the tariff to retail access programs[48] and to state determinations drawing the line between FERC-jurisdictional transmission and state-jurisdictional local distribution facilities.[49] "We intend to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies."[50]

The D.C. Circuit upheld Order 888 in most regards, including FERC's assertion of jurisdiction over unbundled retail transmission: "We are bound by the High Court's dictates to conclude that the FPA gives FERC the authority to regulate the transmissions at issue here, whether retail or wholesale." *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 694 (D.C. Cir. 2000). Enron App. B at 34a. In addition, the D.C. Circuit determined that even absent

[46] *See* Order 888, 61 Fed. Reg. at 21,625-26, Enron App. D. at 304a-308a.

[47] Order 888, 61 Fed. Reg. at 21,725, Enron App. D at 336a. *See also* Part II below and Brief of Enron as Respondent in No. 00-568 at 18-22 for description of transmission on the two interstate grids.

[48] *See* Order 888, 61 Fed. Reg. at 21,627, Enron App. D at 314a; *see also id.*, 61 Fed. Reg. at 21,572, Enron App. D at 231a.

[49] *See* Order 888, 61 Fed. Reg. at 21,626, Enron App. D at 311a.

[50] *See* Order 888, 61 Fed. Reg. at 21,542, Enron App. D at 136a-137a. *See also id.* 61 Fed. Reg. at 21,628, Enron App. D at 314a-315a.

binding precedent, FERC's interpretation would be sustained. *Id.*, Enron App. B at 34a-35a.

SUMMARY OF ARGUMENT

New York and California[51] challenge FERC's determination, as part of its remedy for undue discrimination in interstate transmission service, to assert jurisdiction over the transmission service used to provide retail customers direct access to their choice of a competitive generation supplier. Their arguments cannot overcome the language of the FPA, the inability of individual states to regulate interstate transmission service, and the fact that only federal regulation can provide the non-discriminatory transmission required to support federal policy, as well as the policy of retail choice states, in favor of competitive electricity markets.

To claim state jurisdiction over the unbundled transmission supporting direct sales by competitive suppliers to retail customers, New York and California are forced to read into the FPA language that does not exist and to ignore FPA Section 201(b)'s broad grant of jurisdiction to FERC over the "transmission of electric energy in interstate commerce." The plain language of the FPA is contrary to the States' core premise that the FPA accords FERC jurisdiction only over the interstate transmission associated with wholesale sales. The FPA limits FERC's jurisdiction over sales of electric energy to wholesale sales, but contains no such limitation with respect to FERC's jurisdiction over interstate transmission.

New York's claim that retail electric customers are served by intrastate transmission is a fiction. FERC correctly held, following this Court's precedent, that as a matter of engineering reality, all transmission on the interconnected interstate grid is in interstate commerce. The fallacy of New

[51] New York and California are jointly referred to herein as "the States."

York's characterization is particularly apparent in the context of retail competition programs, whose essence is the empowerment of retail customers to use transmission to access competitive interstate generation markets and deal directly with the suppliers of their choice.

Congress' wisdom in granting FERC plenary authority over transmission in interstate commerce is confirmed by the practical reality that states are unable to regulate the interstate transmission required to support retail customers' direct access to competitive generation markets. State attempts to do so would necessarily leave important gaps. No single state could regulate the transmission required for a retail customer in state A to transact with a competitive generator in state B. Perhaps even more troubling, adoption of the States' position would invite discrimination and lead to conflicts over use of what is necessarily a unitary transmission network. No regulatory authority, state or federal, would have jurisdiction to resolve such conflicts. The result would inevitably thwart retail choice programs in neighboring states and undermine federal policy in favor of competitive interstate electricity markets.

Unlike the states, FERC can and has bridged the gap through its open access tariffs, which provide the means for retail choice customers to obtain the transmission service necessary to reach competitive suppliers, wherever located. The non-discriminatory open access transmission service FERC found essential for competitive electricity markets can only be achieved through a single set of rules, administered by federal authority.

New York's contention that FERC's action invades what had been the exclusive regulatory domain of the states is not only insufficient to overcome the FPA's express grant of authority, but is wrong as a matter of fact. For decades FERC has exercised jurisdiction over unbundled transmission for retail customers in those limited cases where such transmission was provided notwithstanding state-sanctioned

exclusive retail service territories. What is new is not FERC regulation of unbundled transmission for retail customers. Instead, it is the greatly expanded volume of such transmission resulting from state decisions to drastically alter the way electricity is purchased, sold, and regulated.

The States' effort to support their position on policy grounds demonstrates only their failure to grasp or attempt to obscure what is at stake. States adopting retail choice are depending on competitive markets to discipline generation prices to just and reasonable levels. Reliance on competition in lieu of regulation can only succeed in the context of robust interstate markets. FERC's assertion of jurisdiction over the interstate transmission used by retail choice customers is an essential regulatory predicate for ensuring the non-discriminatory access to the interstate transmission grid essential to the competitive interstate markets relied on by retail choice and wholesale customers.

ARGUMENT

I. THE STATES' ANALYSIS DOES NOT COMPORT WITH THE PLAIN LANGUAGE OF THE STATUTE

New York argues that the FPA affords the states jurisdiction over the unbundled transmission service used to facilitate retail sales. According to New York, "§ 201(a) preserves state jurisdiction over retail transmissions." (NY Br. at 40.) California contends that "FERC's jurisdiction does not extend to the part of transmission in interstate commerce that constitutes local distribution." (CA Br. at 3.) Both positions suffer from the same defect. New York and California read the FPA as creating a bright line jurisdictional divide between retail and wholesale sales and between retail and wholesale transmission.

This interpretation founders on the hard shoals of the plain language of the statute. The FPA does divide federal and state jurisdiction over sales along wholesale and retail lines.

No corresponding divide exists with respect to transmission. Fatal to their position, New York and California read the statute to say what it does not say, and ignore what it plainly does says. Nor can their reliance on isolated extracts of legislative history overcome the FPA's express language.[52] Where the statute's language is plain, as here, that is the end of the matter.[53]

New York also argues that the unbundled transmission service supporting retail electric sales is not transmission of electric energy in interstate commerce. (NY Br. at 45 n.28.) This contention is contrary to FERC's expert determination, applicable precedent of this Court and lower courts, and wrong. California apparently agrees with FERC, and concedes "the expansive nature of 'transmission in interstate commerce' when electric systems are interconnected." (CA Br. at 22.)

A. Section 201(b)(1) Grants FERC Jurisdiction Over All Transmission of Electric Energy In Interstate Commerce, Not "Wholesale Sales and Associated Transmission In Interstate Commerce"

Section 201(b)(1) of the Federal Power Act grants FERC jurisdiction over "the transmission of electric energy in interstate commerce."[54] In explaining its legal authority to place unbundled retail transmission under the rates, terms, and conditions of the *pro forma* tariff, FERC correctly found this statutory language "compelling." Order 888, 61 Fed. Reg. at 21,625, Enron App. D at 305a. "[S]ection 201 of the FPA, *on its face*, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities)

---

[52] *See* Brief of Enron as Respondent in No. 00-568 at 25-28.

[53] Where "the statute's language is plain, 'the sole function of the courts is to enforce it according to its terms.'" *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 241 (1989) (quoting *Caminetti v. United States*, 242 U.S. 470, 485 (1917)).

[54] 16 U.S.C. § 824(b)(1).

without qualification." *Id.* (emphasis in original). Separate and independent of the grant of authority over transmission in interstate commerce, Section 201(b)(1) also provides FERC jurisdiction over "the sale of electric energy at wholesale in interstate commerce."

New York studiously avoids the relevant language of Section 201(b)(1). Only twice in its brief, in the recitation of the "Statutory Provisions Involved" (NY Br. at 2), and in passing (*id.* at 40), does New York even quote the statutory language that FERC stands on. Instead, New York repeatedly, and erroneously, contends that the "FPA[] authoriz[es] FERC to regulate wholesale sales *and associated transmission* in interstate commerce." (*Id.* at 7 (emphasis supplied). *See also id.* at 26 ("Associated Transmissions") and 30-31 ("transmissions associated with wholesale transactions").)

Section 201(b) leaves no portion of interstate transmission by public utilities to the states' jurisdiction. The delegation of authority to FERC is exclusive and comprehensive. Section 201(b) expressly distinguishes between FERC's regulatory authority over the transmission of electric energy in interstate commerce and the additional provision of FERC jurisdiction over "the sale of electric energy at wholesale in interstate commerce...." Unlike its jurisdiction over sales of electricity, FERC's jurisdiction over transmission is not limited to transmission of electrical energy associated with a wholesale sale. The necessary conclusion is that Congress intended no such limitation on the scope of FERC's jurisdiction over interstate transmission. *See Bates v. United States*, 522 U.S. 23, 29-30 (1997).

Section 201(b)(1) states that Part II of the FPA shall apply to (and thus FERC shall have jurisdiction over) "*the* transmission of electric energy in interstate commerce."[55] The use of the definite article "the" clearly indicates that

[55] 16 U.S.C. § 824(b)(1) (emphasis supplied).

there is only one body of interstate electrical transmission and that all of it is FERC jurisdictional. Section 201(b)(1)'s complete grant of jurisdiction to FERC over "the" subject of interstate electric transmission cannot be reconciled with New York's and California's respective contentions that some portion of interstate transmission is reserved to the states under Section 201(a) or constitutes state-regulated "local distribution" under 201(b)(1).

The phrase "transmission ... in interstate commerce" appears throughout Section 201. Consistent with Section 201(b)(1), Section 201(a) expressly provides for "Federal regulation ... of the transmission of electric energy in interstate commerce," and differentiates this regulatory authority from FERC's jurisdiction over "the sale of such energy at wholesale in interstate commerce."[56]

Section 201(c) defines "interstate transmission" that FERC regulates under Section 201(b)(1) (and Part II of the FPA) as "electric energy ... transmitted from a State and consumed at any point outside thereof."[57] Tellingly, and consistent with Sections 201(a) and 201(b), Section 201(c) nowhere limits FERC's jurisdiction to transmission associated with wholesale sales. In drafting Section 201 and Part II of the Federal Power Act, Congress could have easily limited FERC's jurisdiction over interstate transmission to transmission associated with wholesale sales. It did not do so. Instead, Section 201(b) sweepingly and exhaustively grants FERC jurisdiction over the transmission of all electrical energy in interstate commerce by public utilities.

Although New York (NY Br. at 45) contends that the plain language of Section 201(c) supports its position, New York's

[56] 16 U.S.C. § 824(a).

[57] Section 201(c) provides in full: "For the purpose of this Part, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof: but only insofar as such transmission takes place within the United States." 16 U.S.C. § 824(c).

reading is predicated upon a factual contention rejected by FERC and this Court, *i.e.*, that there are separate streams of interstate and intrastate electrons on the interconnected interstate grid supplying discrete individual loads. *See* Part II *infra*. FERC properly determined that all transmission of electricity on the interconnected grid, including unbundled retail transmission, is in interstate commerce within the meaning of Section 201(c).

B. The General Policy Declaration of Section 201(a) Cannot Undermine The Specific Grant of Jurisdiction To FERC Under Section 201(b)(1)

New York argues that Section 201(a) of the FPA preserves state jurisdiction over "retail transmission ... that [was] being regulated by the states in 1935." (NY Br. at 33.) California argues that "any reasonable doubt" as to FERC's exercise of jurisdiction over unbundled retail transmission must be exercised against FERC pursuant to "Section 201(a)'s rule of construction." (CA Br. at 26.) The States are wrong.

As a matter of statutory interpretation, the States' Section 201(a) arguments falter against the express grant of jurisdiction in Section 201(b). Under basic canons of statutory construction, and as this Court has held, the exhortatory provisions of Section 201(a) cannot subvert Section 201(b)'s specific grant of authority. Section "201(a) was merely a 'policy declaration ... of great generality. It cannot nullify a clear and specific grant of jurisdiction, even if the particular grant seems inconsistent with the broadly expressed purpose.'" *FPC v. Southern California Edison Co.*, 376 U.S. 205, 215 (1964) ("*Colton*") (quoting *Connecticut Light & Power Co. v FPC*, 324 U.S. 515, 527 (1945)). California concedes that Section 201(a) is a "policy provision" and cannot "nullify a clear and specific grant of jurisdiction." (CA Br. at 25 (quoting *CL&P*, 324 U.S. at 527).) Because Section 201(b)(1) expressly grants FERC jurisdiction over the transmission of electricity in interstate

commerce, *Colton* disposes of the States' Section 201(a) arguments.

C. The Plain Language Distinguishes Between Interstate Transmission and Local Distribution

Unlike New York, California addresses the critical language of Section 201(b) and acknowledges that the phrase "transmission ... in interstate commerce" as used in Section 201(b) encompasses transmission used to support wholesale and retail sales. Thus, California concedes the fundamental premise of FERC's exercise of jurisdiction over unbundled retail transmission. However, California equates "transmission ... service to retail customers" with the phrase "local distribution." (CA Br. at 16.) California contends that "local distribution is ... *a subset* ... of transmission in interstate commerce." (*Id.* at 8 (emphasis supplied).) California seizes on Section 201(b)(1)'s grant of state jurisdiction "over facilities used in local distribution" and attempts to read this language as an excepted "subset" to the otherwise plenary grant of jurisdiction to FERC over the transmission of electric energy in interstate commerce. Contrary to California, the statute creates no excepted "subset."

California confuses jurisdiction over local distribution with jurisdiction over transmission. It is a basic tenet of statutory construction that where different words are used they are intended to mean different things. Here, different subjects are at issue, jurisdiction over "local distribution" as opposed to jurisdiction over "transmission."[58] FERC recognizes the

---

[58] Although subject to case-by-case review under FERC's "seven factor" test, Order 888, 61 Fed. Reg. at 21,625, Enron App. D at 307a-310a, the distinction between transmission and local distribution facilities is generally recognized. In its August 19, 1999 initial appellate brief below (at 3), New York observed that "[t]he key distinction between transmission facilities and local distribution facilities is that local distribution facilities normally provide one-way power to serve end-users. ... [P]ower does not flow from a local distribution system to other such

states' jurisdiction to regulate local distribution. Order 888, 61 Fed. Reg. at 21,619, Enron App. D at 281a. Underscoring the legislative awareness of the distinction between "transmission" and "local distribution," Section 201(b)(1) provides the states an express reservation of jurisdiction over transmission, where used "*only for* the transmission of electric energy in *intrastate commerce*" (emphasis supplied). The parallel distinction between this limited grant of state jurisdiction and the federal grant of jurisdiction over "the transmission of electric energy in interstate commerce" is marked, compelling, and logical. Congress provided a plenary grant of jurisdiction to FERC to regulate transmission in the federal domain of interstate commerce. FERC has grown into this transmission jurisdiction with the expanding interconnection of the grid, and changes in both the industry and the way electricity is bought and sold.

California, like New York, must read language into the statute that does not exist. The "ordinar[y]" practice is to "resist reading words or elements into a statute that do not appear on its face." *Bates*, 522 U.S. at 29. The FPA does not say that FERC has only "some" jurisdiction over the transmission of electricity in interstate commerce or in any way suggest that FERC's transmission jurisdiction is limited by the states' jurisdiction over local distribution facilities. In an attempt to surmount this daunting hurdle, California contends that the phrase "local distribution" is essentially a term of art that includes retail transmission. (*See, e.g.*, CA Br. at 10-11.) California grounds its misinterpretation of the statute upon a misreading of *CL&P*, the principal authority on which it seeks to rely. The issue in *CL&P* was whether CL&P was a FERC-jurisdictional "public utility."[59] What

systems. A transmission system usually ends at a substation where transformers reduce power voltages to lower levels for local distribution." *See also CL&P*, 324 U.S. at 534.

[59] The Court explained that "such regulation depend[ed] on whether [CL&P possessed] facilities ... under the jurisdiction of the Commission." *CL&P*, 324 U.S. at 528. The Court remanded to FERC

was not before the Court, and what *CL&P* did not address, was a contention that Connecticut would have had jurisdiction over all transmission supporting CL&P's retail sales if CL&P had local distribution facilities that were involved in the delivery of electricity transmitted in interstate commerce. California cites no apposite authority for this proposition, and to the best of TAPS' knowledge there is none.

Indeed, in addressing the Natural Gas Act ("NGA"), a statute to be construed *in pari materia* with the Federal Power Act,[60] this Court has held to the contrary. In *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621 (1972), the Court addressed FERC's jurisdiction over gas transportation under Section 1(b) of the NGA,[61] the counterpart grant of jurisdictional authority to Section 201(b) of the FPA. The Court held that "though the Act's application to 'sales' is limited to sales of interstate gas for resale, the Act applies to interstate 'transportation' regardless of whether the gas transported is ultimately sold retail or wholesale." *LP&L*, 406 U.S. at 636 (citation omitted). Regardless of New York and California's different paths of analysis (*viz.*, under the

the determination whether the facilities identified as the basis for exerting jurisdiction were instead local distribution facilities such that FERC would not have jurisdiction over CL&P as a "public utility." *Id.* at 532-33. The *CL&P* Court explained that "once a company is properly found to be a 'public utility' under the Act the fact that a local commission may also have regulatory power does not preclude exercise of the Commission's functions." *Id.* at 533. The Court distinguished, but apparently understood to be good law on this point, *In the Matter of Hartford Elec. Light Co.*, 2 F.P.C. 502 (1941), *aff'd sub nom. Hartford Elec. Light Co. v. FPC*, 131 F.2d 953 (2d Cir. 1942). The Second Circuit noted that "[Section] 201(b), disjunctively, confers jurisdiction over interstate transmission or interstate wholesale sales," and that to find otherwise could create a regulatory gap "in flat contradiction of the legislative purpose." 131 F.2d at 965.

[60] *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981).

[61] 15 U.S.C. § 717(b).

reservation of Section 201(a) or the local distribution language of Section 201(b)), *LP&L* is a clear and direct rejection of the States' fundamental premise that FERC's jurisdiction over interstate transmission is limited to transmission associated with wholesale sales.[62]

D. The Language of Section 206(d) Does Not Support the States' Position

New York seeks to rely upon FPA Section 206(d),[63] (formerly Section 206(b)) as a demonstration that Congress intended to limit the Commission's role with regard to the transmission component of retail sales to merely providing information at the request of a state. (*See* NY Br. at 12; NY Respondent Br. at 17.) California (CA Br. at 17) casts Section 206(d) as "limited assisting authority," enabling FERC to provide states with the cost of out-of-state facilities used to provide in-state retail service. To the contrary, Section 206(d) further undermines the argument that Congress intended to preserve the states' jurisdiction over all aspects of retail service.

The States' reading of Section 206(d) fails to recognize the authority it expressly provides the Commission "on its own motion" to "determine" transmission cost even where it has

[62] Contrary to California (CA Br. at 24) and New York (NY Respondent Br. at 15), the Hinshaw Amendment to the NGA (codified at 15 U.S.C. § 717(c)) neither supports the States' reading of the FPA nor serves to distinguish *LP&L*. The Hinshaw Amendment, to which there is no parallel provision under the FPA, was "intended to exempt ... persons from FERC regulation only for the purposes of their involvement in intrastate gas transport, not for the purposes of their involvement in interstate ... regulated activities." *Public Utilities Comm'n of California v. FERC*, 143 F.3d 610, 615 (D.C. Cir. 1998). *LP&L* rests upon this Court's determination that the Commission, and not the states, regulates interstate transport regardless of whether the associated sale is at wholesale or retail. Further, the fact that there is no equivalent in the FPA to the Hinshaw Amendment makes the States' argument suspect at best.

[63] 16 U.S.C. § 824e(d).

no authority to set the rate for the ultimate sale.[64] The Commission is not limited to taking action under Section 206(d) only on the request of a state. The Commission's action under Section 206(d) also is not restricted to mere provision of assistance or information, as highlighted by the use of the term "determine," the same term used in Section 206(a).[65] Nor is FERC's Section 206(d) authority confined to out-of-state facilities, as California suggests.

Thus, Section 206(d) affords FERC the ability to "determine" the transmission component of even bundled sales rates set by the states. *Cf. Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986). It cannot support an argument that where a state elects to let the competitive interstate market discipline the generation component of retail electricity prices, and to break out the interstate transmission that retail customers must use to gain direct access to that market, FERC is without authority to regulate the rates, terms, and conditions of that transmission under Sections 205(d) or 206(a).

[64] Section 206(d) provides (emphasis supplied):

> The Commission *upon its own motion*, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may *investigate and determine* the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

[65] Section 206(a) provides that "[w]henever the Commission ... shall find that any rate, charges or classification ... for any transmission or sale subject to the jurisdiction of the Commission, ... is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall *determine* the just and reasonable rate, charge, classification ... to be thereafter observed and in force and shall fix the same by order." 16 U.S.C. § 824e(a) (emphasis supplied).

E. Sections 211 and 212 Do Not Support The States' Position

FPA Sections 211 and 212, as amended by EPAct, further demonstrate the breadth of the grant of jurisdiction to FERC over interstate transmission under Section 201(b)(1). Section 211 grants FERC certain wheeling authority where Section 212 conditions are met. Section 212(a) expressly provides that that wheeling authority is limited to ordering "wholesale transmission service."[66] Congress would have had no need to differentiate in Section 212 between "wholesale" and "retail" transmission if FERC's regulatory authority over "the transmission of electric energy in interstate commerce" was already limited to the provision of only wholesale transmission service, *i.e.*, what New York describes as transmission associated with wholesale transactions. Nothing in Sections 211 or 212 limits FERC's authority under Sections 205 and 206 to regulate unbundled transmission provided voluntarily for retail customers or pursuant to a state retail access program. Section 212(e) is a savings provision, which states that "[e]xcept as provided in section 210, 211, 214, or [212], such sections shall not be construed as limiting or impairing any authority of the Commission under any other provision of law."[67]

To like effect, Section 212(h)'s prohibition against FERC's ordering retail wheeling would be wholly nugatory if FERC did not otherwise have authority under Section 201(b)(1) over interstate transmission associated with retail transactions. Section 212(h) provides that "[n]o order issued under this Act shall ... require the transmission of electric energy ... directly to an ultimate customer."[68] By restricting FERC's authority to order retail wheeling, Section 212(h) merely maintains a state's authority to determine how to regulate the retail sale; FERC cannot require a state to permit

[66] 16 U.S.C. § 824k(a).
[67] 16 U.S.C. § 824k(e).
[68] 16 U.S.C. § 824k(h).

unregulated suppliers to sell power directly to retail consumers, in competition with and through the transmission system of the franchised vertically integrated monopolist. But nothing in Section 212(h) detracts from FERC's authority to regulate the rates, terms, and conditions of the interstate transmission service that a state authorizes retail customers to use to deal directly with competitive generation suppliers.

II. FERC CORRECTLY FOUND THAT ALL TRANSMISSION ON THE INTERCONNECTED GRID IS IN INTERSTATE COMMERCE

Based upon its institutional expertise, and grounded in the precedent of this Court, FERC properly determined that all transmission of electric energy on the interconnected grid is transmission in interstate commerce. Addressing specifically the Commission's jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce, FERC held that "[b]ecause of the highly integrated nature of the electric system, this results in most transmission of electric energy being 'in interstate commerce.'" Order 888, 61 Fed. Reg. at 21,725, Enron App. D at 336a. FERC made clear that intrastate transmission occurred only on those electric systems that FERC determined to be not "interconnected" with the interstate grid, *i.e.*, Alaska, Hawaii and those portions of Texas that are linked to the rest of the grid only through direct current ties. *Id.*, 61 Fed. Reg. at 21,625 n.541, Enron App. D at 305a n.541.

New York disputes FERC's factual determination. To prevail, New York must show that there exist discrete transmissions of electricity from within state generators to within state loads. New York claims that "*most* energy passes from power plants to the retail customers who are first in line on transmission lines with suitable capacity" (NY Br. at 45 n.28 (emphasis supplied).) But even New York's assertion necessarily implies that at least *some* energy is always being

supplied to loads from remote, including out-of-state, generators.

More fundamentally, New York's attack on FERC's expert determination conflicts with findings of this Court and numerous lower courts recognizing the scientific and engineering fact that modern interconnected electric systems operate as an integrated network, instantaneously linking multiple generating resources to multiple consuming loads, such that all loads draw from a pool of common and commingled electrons.[69] For example, in *New England Power Co. v. New Hampshire*, 455 U.S. 331 (1982), this Court recognized that as a matter of engineering New Hampshire could not stop the physical flow of electricity in or out of the state without "sever[ing] ... connections with the [New England] Power Pool." *Id.* at 336. "So long as the electricity produced at New England Power's hydroelectric plants continues to flow through the Pool's regional transmission network, it will be impossible to contain that electricity within the State of New Hampshire in any physical sense." *Id.* Similarly, in *Arkansas Power & Light Co. v. FPC*, 368 F.2d 376 (8th Cir. 1966), the court affirmed FERC's determination that "generation from each source in the system contributes directly or indirectly, and to an ever varying extent, to the energy present in all parts of the system which are not isolated from out-of-state energy sources." *Id.* at 382 (citation omitted).

FERC and the court of appeals below properly relied upon *FPC v. Florida Power & Light Co.*, 404 U.S. 453, 461 (1972) as support for the determination that the interconnection of modern electric systems results in a "coming[ling]" of electrons in a common "reservoir." The scope of this holding was not lost on Justice Douglas writing

[69] *See also Public Serv. Co of Colorado*, 62 F.E.R.C. ¶ 61,013, at 61,061 (1993) (high voltage transmission facilities are integrated into a "cohesive network moving energy in bulk," which "operates as a single piece of equipment").

in dissent *id.* at 471, *viz.*, that FERC had plenary jurisdiction over the transmission of "every privately owned interconnected [utility] in the United States."[70] *FPL* rejects New York's contention that it is scientifically possible to exactingly trace the flow of electrons from a specific generator to a specific load on a highly integrated multi-state grid. "Logic would seem to dictate that where the utility ... has continuous access to an integrated pool of interstate energy, the tracing of out-of-state energy is indeed difficult, burdensome, and perhaps impossible." *Id.* at 468 n.18 (quoting *Arkansas Power*, 368 F.2d at 382).

New York's attempt to distinguish *FPL* as an accounting case (NY Br. at 42-44) is rebutted by *FPL* itself. In affirming FERC's determination that FPL was a public utility subject to Part II regulation, this Court upheld the Commission's order below that FPL "must comply with all ... requirements of the Commission's Regulations under [the FPA]." *Florida Power & Light Co.*, 37 F.P.C. 544, 546 (1967), *aff'd*, 404 U.S. 453.

New York's depiction of intrastate transmission on the eastern and western grids is a fantasy that defies scientific truth and common experience. Perhaps nothing brings home the interconnected and integrated nature of the grid more dramatically than system failures. As explained in the Commission's Report to the President concerning the 1965 Northeast blackout, the "Northeast power failure began at approximately 5:16 p.m. on November 9, 1965, and by 5:30 p.m. most of the northeastern United States ... was in darkness.... The failure encompassed 80,000 square miles ... and directly affected an estimated 30 million people in the

[70] It is immaterial whether *FPL* rested on "one or more electrons" being in interstate commerce. (NY Br. at 42 n.25.) Justice Douglas's criticism of *de minimis* power flows is plainly a relic of the past. Since *FPL* was decided, Florida Power & Light has directly integrated its operations with utility operations in Georgia by means of 500 kv transmission facilities. *Florida Power & Light Co.*, 27 F.E.R.C. ¶ 61,333, at 61,641 (1984).

United States and Canada."[71] As utility systems became electrically isolated in response to the power surge they were left with insufficient resources to serve load, leading to blackout.

> The second stage [of the blackout] marked the attempted survival of the electric utilities in eastern New York and New England which had been separated from the rest of the interconnected systems of the United States. Isolated from other systems, these "islands" ... generally were left with insufficient generation to meet their loads. Power generation in virtually all of this area ... ceased within a matter of three to twelve minutes.

Report at 7-8. The western grid has also suffered catastrophic blackouts. In August 1996 a transmission failure caused by sagging transmission lines in Oregon resulted in a power outage that cut electricity to more than four million people in nine Western states.[72]

Given the interconnected and highly integrated nature of the electric grid, New York's notion that loads connected to the integrated high voltage grid are served separately from within-state generation is simply false. It rings particularly hollow in the context of the unbundled transmission service required to support retail customer access to competitive interstate generation markets.

---

[71] Federal Power Commission, Vol. 1 – Report of the Commission, Prevention of Power Failures at 7 (July 1967).

[72] "Officials said the weakened grid knocked out the four main power highways that send electricity to the other states, causing a virtual domino effect." CNN, *Sagging power lines, hot weather blamed for blackouts*, CNN Interactive, Aug. 11, 1996, *at* http://www.cnn.com/US/9608/11/power.outage.

III. ONLY FERC IS COMPETENT TO REGULATE INTERSTATE TRANSMISSION

To the extent there is any ambiguity concerning FERC's FPA authority to regulate unbundled transmission to retail customers, the matter must be resolved in FERC's favor. FERC is competent to regulate unbundled retail transmission as a matter of interstate commerce; the states are not.

> [W]hen a dispute arises over whether a given transaction is within the scope of federal or state regulatory authority, we are not inclined to approach the problem negatively, thus raising the possibility that a 'no man's land' will be created. ... [W]here congressional authority is not explicit we must ask whether state authority can practicably regulate a given area and, if we find that it cannot, then we are impelled to decide that federal authority governs.

LP&L, 406 U.S. at 631 (quoting *FPC v. Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 19-20 (1961)).

New York and California assert that the states can regulate unbundled "retail transmission" that is in interstate commerce. Remarkably, neither addresses where the scope of this purported jurisdiction ends. New York states (NY Br. at 6 n.2) that what it means by "retail transmission" is defined in the Glossary of Terms contained in New York App. Q. Appendix Q defines "retail transmission service" to encompass all "[t]ransmission provided to a retail customer." (NY App. Q-3.) Where a state unbundles transmission and allows retail customers access to competitive electricity markets, this definition could encompass transmission service by numerous utilities, stretching across several states. California defines "retail transmission" to mean "the utility's use of its own transmission and other facilities to deliver electric power to the retail customer at the place of end use." (CA Br. at 6 n.4.) This definition is problematic in

several respects. The unbundled transmission service necessary to support a competitive retail sale may require the use of multiple utilities' transmission facilities. In addition, the transmission facilities of a particular utility may extend over multiple states.

Even cursory analysis makes clear that the states are not able to regulate interstate transmission associated with an unbundled retail sale. For example, no state could regulate the transmission service required for the direct sale from a generator in Oregon to an end use customer in California. California has no power to regulate that portion of the transmission arrangement that moves over transmission facilities in Oregon, and Oregon is equally powerless to regulate the California leg of the transmission.

> [A] statute that directly controls commerce occurring wholly outside the boundaries of a State exceeds the inherent limits of the enacting State's authority and is invalid regardless of whether the statute's extraterritorial reach was intended by the legislature. The critical inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State.

Healy v. The Beer Institute, 491 U.S. 324, 336-37 (1989).

Unlike the states, FERC *can* regulate the multi-state transmission service necessary for suppliers and retail customers to avail themselves of competitive generation markets. FERC correctly determined that a uniform tariff was necessary to ensure competitive markets and avoid balkanization. FERC's *pro forma* tariff is the bridge that transcends the unworkable gaps in state regulation of unbundled retail transmission. Under Section 1.11 of the *pro forma* tariff, "any retail customer taking unbundled Transmission Service pursuant to a state retail access program" is an "Eligible Customer" entitled to open access transmission service. Order 888, 61 Fed. Reg. at 21,708.

Thus, under the tariff, a customer in state A, which has authorized retail customers to directly access competitive generation markets, can obtain the transmission service necessary to reach any willing supplier in state B (or C, or D), and the entire transmission arrangement is governed by the FERC *pro forma* tariff regardless of state boundaries. States that have implemented retail competition should welcome the necessary ingredients of FERC regulation and the *pro forma* tariff so that their residents can access competitive interstate markets and out-of-state resources.

State regulation of the interstate transmission necessary to provide retail customers access to competitive interstate markets is inherently unworkable. Through the *pro forma* tariff, FERC has provided a uniform transactional and operational schema to address, *inter alia*, matters of transmission (including interface) capacity, scheduling, reservation, priority rights, available types of service, curtailment, and pricing. Permitting a state to regulate transmission for its retail customers differently from FERC's regulation of transmission for wholesale customers and out-of-state retail customers[73] creates conflicts that will paralyze the grid and cripple the interstate electricity markets on which retail access programs necessarily rely. The inevitable result would be conflicting claims over rights to use what is necessarily a single integrated transmission system, with *no* regulatory body in a position to resolve those claims.

FERC's *pro forma* tariff provides a "first-come first-served" system for reservation of long term "firm" (non-interruptible) transmission capacity.[74] If states had authority

---

[73] Under New York's definition of "retail transmission," this retail transmission apparently would be regulated by other states (and not FERC), but regulation of retail transmission by a multiplicity of individual states only aggravates the problem of conflicting regulation.

[74] *See* Order 888, Tariff § 13.2, 61 Fed. Reg. at 21,711, which establishes the first-in-time reservation priority for "point-to-point" service (where a customer reserves a specified amount of transmission from designated

to set the rates, terms, and conditions of unbundled transmission service for retail customers, each state could establish a different rule for reserving use of the same transmission interstate facilities that are governed by FERC's tariff. The inevitable result would be impairment of competitive interstate markets, and degradation of reliability.

For example, state A could establish a rule that its retail customers are entitled to have their transmission requests satisfied first, with previously submitted transmission requests of wholesale customers and retail customers from neighboring states accorded only leftover capacity. Assume an interface between a utility in state A and a utility in state B can safely accommodate 100 MW of transfers from state B into state A, and that unbundled retail customers from state C (that were importing power from state B through state A) and wholesale customers already had reserved 60 MW of that import capacity. If state A's retail customers later seek to reserve another 60 MW under state A's "my retail customers come first" rule, then the interface could not carry all the transactions that are properly confirmed under FERC's reservation regime and state A's rule without threatening reliability or safety. If, to protect the transmission system from an overload, the state A utility followed state A's rule and curtailed the wholesale and state C retail customers, leaving those customers without a source of power, competitive interstate markets would be undermined. In addition, state A's rule would thwart state C's policy decision to rely on direct access by retail customers to competitive interstate markets to ensure just and reasonable

points of receipt (where the energy is deemed to enter the grid) to designated points of delivery (where energy is deemed to leave the grid by contractually being delivered into a neighboring system or distribution facilities)). Section 13.2 accords point-to-point customers equal reservation priority with designations made for "Network Service" (where a customer reserves service by designating "Network Resources" to serve its designated "Network Load"), as well as "Native Load Customers" (which include bundled retail and wholesale load).

retail electricity prices. Imposition of retaliatory preference rules by state C would not be hard to imagine.[75]

In its Brief as Respondents (NY Respondent Br. at 18), New York unwittingly concedes that individual state regimes for reserving transmission service will not work. New York argues against the potential for discrimination against wholesale users by relying on Order 888's limits on the ability of vertically integrated utilities to reserve capacity for bundled retail load growth. Yet, by asserting the authority to regulate the rates, terms and conditions (without apparent exception) of unbundled retail transmission service, New York claims the rights to impose a reservation regime different than FERC's regime (and different than other states), inviting discrimination and jurisdictional conflicts over use rights.

Similarly, if the States are correct, they could establish a curtailment priority for unbundled retail transmission service that conflicts with the *pro rata* curtailment priority established by FERC's open access tariff. California (CA Br. at 29-30) recognizes the "common[]" state practice, "when transmission is short," of "requir[ing] electric utilities to protect first the retail customers to whom public utility obligations are owed" and argues against FERC authority over unbundled retail transmission because it would enable FERC to "implement its different policy for retail customers directly." California thus highlights the potential, if the States' position is adopted, for each state to discriminate in favor of its own retail customers, while subordinating the rights of wholesale and out-of-state retail users. Such parochialism will defeat retail access programs in

[75] State imposition of a queuing mechanism for interruptible retail transmission service that differs from the mechanism applicable under Section 14.2 of the *pro forma* tariff (which provides for ranking based on duration and pricing), Order 888, 61 Fed. Reg. at 21,712, also could cause havoc.

neighboring states, and undermine the competitive electricity markets Congress has sought to promote.

As California correctly concedes (CA Br. at 8 n.5), electricity is instantaneously generated, transmitted, and consumed. To access competitive markets, all users must rely on the same integrated transmission grid. Perhaps no other industry stands more in need of a single set of interstate rules, and a single traffic cop, to ensure the coordinated, non-discriminatory, and efficient use of the transmission required to support competitive electricity markets. For example, it would be inconceivable for Virginia to establish a rule that during rush hours, out-of-state vehicles on Interstate 95 must pull over to the shoulder so Virginia vehicles may pass. *Cf. Buck v. Kuykendall*, 267 U.S. 307 (1925).[76] But that is precisely what the "commonly" applied state curtailment practice touted by California (CA Br. at 29-30) would invite with regard to interstate transmission highways.

State regulation of interstate transmission creates an impermissible risk of unlawful protectionism. Each state "would be obliged to regulate in the State, not the national interest." *LP&L*, 406 U.S. at 633. The inevitable conflict of high cost and low cost states "will create contradictory regulations that cannot possibly be equitably resolved by the courts." *Id.* at 634. Cries for state protectionism have already been sounded in California.[77] By regulating transmission for

[76] *Buck* struck down an Oregon law prohibiting interstate carriers from using certain highway routes. The law impermissibly regulated "the persons by whom the highways may be used. It prohibits such use to some persons while permitting it to others for the same purpose and in the same manner." *Buck*, 267 U.S. at 315-16.

[77] A.B. 6 § 3, 2001 Leg., 1st Ex. Sess. (Cal. 2001) (enacted), amends Section 377 of the California Public Utilities Code to provide that the California Public Utilities "commission shall ensure that public utility generation assets remain dedicated to service for the benefit of California ratepayers." This would appear to ban the export of power. In his State of the State address Governor Davis is reported as stating that "there's no point in building more plants in our state if the electricity will flow out of our state." Governor Gray Davis, State of the State Address (Jan. 8, 2001), *text available at* http://www.governor.ca.gov/state/govsite/gov_homepage.jsp.

unbundled retail customers, any state could effectively shut down the import and export of electricity for competitive sales at wholesale and retail, as well as "through traffic." But no such protectionist authority over competitive interstate markets was reserved to the states under the FPA. The states cannot "restrict the flow of privately owned and produced electricity in interstate commerce, in a manner inconsistent with the Commerce Clause." *New England*, 455 U.S. at 344.[78] The importance of the Commerce Clause, U.S. Const. art. I, § 8 cl. 3, has been manifest in matters like this since *Gibbons v. Ogden*, 22 U.S. 1 (1824).

FERC's purpose in regulating unbundled transmission for retail customers was to avoid balkanizing the interstate transmission of energy. Order 888, 61 Fed. Reg. at 21,627, Enron App. D at 315a. FERC recognized that in doing so it was addressing newly competitive markets. Order 888-A, 62 Fed. Reg. at 12,369, Enron App. E at 476a-477a. California's response is a *non sequitur*. California asserts that the states "are free under the Federal Power Act to maintain ... 'balkanization' and 'discrimination' in the retail power market, *by retaining the traditional system of monopoly utility service* and regulation for retail power." (CA Br. at 20 (emphasis supplied).) Even if California's characterization of FERC's jurisdiction over the transmission component of

[78] New York is wrong to argue that because Congress in 1935 did not foresee retail competition and unbundled retail transmission, it must be presumed that regulation over this interstate transmission was left to the states. (NY Br. at 30.) Matters reserved to the states under the FPA are subject to the restrictions of the Commerce Clause. *New England*, 455 U.S. at 343. Because state regulation of such interstate transmission would run afoul of the Commerce Clause, it is instead presumed that the federal authority granted under FPA Section 201(b) governs. *LP&L*, 406 U.S. at 631.

bundled retail sales were accepted,[79] it cannot justify extending that ability to discriminate to states that have abandoned "the traditional system of monopoly utility service" in favor of retail competition and unbundled transmission service. A state cannot provide its retail customers direct access to competitive interstate markets and then "discriminate[] against interstate commerce ... [in] favor [of] in-state economic interests over out-of-state interests." *Healy*, 491 U.S. at 337 n.14 (quoting *Brown-Foreman Distillers Corp. v. New York*, 476 U.S. 573, 579 (1986)).

IV. FERC'S ASSERTION OF JURISDICTION DID NOT INVADE EXCLUSIVE STATE DOMAIN

A. FERC Has Regulated Unbundled Retail Transmission For Decades

California contends that the states have historically regulated "100% of retail transmission." (CA Br. at 2.) To like effect, New York claims that for 80 years the states have regulated "all aspects of retail deliveries," including retail transmission. (NY Br. at 16.) This is not correct. For decades, FERC has regulated unbundled transmission service to retail customers under FERC-jurisdictional tariffs. Reported cases describing such service are relatively small in number, because prior to the recent introduction of retail competition and due to state franchise restrictions, there were few instances where FERC-jurisdictional public utilities provided unbundled transmission service for end use customers. Nevertheless, prior to Order 888, FERC regulated such transmission in circumstances involving: (1) state retail choice programs; (2) governmental power authorities authorized to provide service to certain end use customers (notwithstanding state territorial laws); and (3) agreements where utility A obtains transmission service over utility B's

[79] The scope of FERC's jurisdiction over the transmission use for bundled retail sales is at issue in No. 00-809.

transmission system to reach utility A's remote retail customers.

FERC regulated unbundled retail transmission service in both New York and California long before Order 888. Beginning in 1975, and pursuant to FERC Rate Schedule No. 95, the Niagara Mohawk Power Corporation ("NIMO") provided transmission service to the New York Power Authority ("NYPA")[80] to serve "six ... industrial customers in Niagara Mohawk's service territory." *Power Auth. of New York v. Niagara Mohawk Power Corp.*, 79 F.E.R.C. ¶ 61,159, at 61,744 (1997). NYPA obtained the right to serve these industrials "pursuant to a 1968 state retail access program authorized by ... New York Public Authorities Law (PAL) sections 1001 and 1005." *Id.* As further shown by its filing at FERC to increase transmission rates, NIMO conceded and FERC accepted the Commission's jurisdiction over NIMO's unbundled transmission service for NYPA's retail customers. *Niagara Mohawk Power Corp.*, 34 F.E.R.C. ¶ 61,028 (1986).

Similarly, in 1981, the Commission found that it (and not New York) had jurisdiction over Consolidated Edison's provision of unbundled transmission service to NYPA's end use customer, the Port Authority of the State of New York. *Consolidated Edison Co. of New York, Inc.*, 15 F.E.R.C. ¶ 61,173, at 61,405 (1981).[81]

Another example of FERC's exercise of jurisdiction over transmission service for retail customers in New York prior

[80] NYPA is also referred to as the Power Authority of the State of New York.

[81] FERC accepted the parties' agreement to permit the New York Public Service Commission to act as initial "arbiter" of the transmission rates. *Consolidated Edison*, 15 F.E.R.C. at 61,405. FERC did so as a matter of administrative convenience expressly subject to FERC's own independent analysis of the rates and FERC's determination that the rates were not unduly discriminatory within the meaning of the FPA. *Id.* at 61,405-06.

to Order 888 is FERC Rate Schedule 165, a transmission service agreement between New York State Electric and Gas Company and NIMO.[82] NYSEG provided firm transmission service to NIMO to permit NIMO's generation and resources to serve NIMO's "remote [retail] loads" which were connected to NYSEG's transmission system. *Niagara Mohawk Power Corp.*, 82 F.E.R.C. ¶ 63,018, at 65,136 (1998) (initial decision), *aff'd in relevant part*, 92 F.E.R.C. ¶ 61,168 (2000).

FERC also regulated unbundled retail transmission in California pre-Order 888. In *Pacific Gas & Elec. Co.*, 56 F.E.R.C. ¶ 61,322 (1991), FERC rejected PG&E's attempt to terminate transmission service for the Western Area Power Administration ("WAPA") that enabled the federal power marketing agency to serve its end use customer, the Lawrence Livermore National Laboratory. FERC explicitly rejected PG&E's claim that the service provided was pursuant to "PG&E's standby retail power tariff." *Id.* at 62,289. FERC found that "[t]ransmission service provided by PG&E to WAPA and its customers under the contract must be provided at the [FERC] filed rate which is applied to energy flows to Livermore over PG&E's lines." *Id.* at 62,291 (footnote omitted). Pursuant to a 1967 agreement (Contract 2948A), PG&E transmits WAPA's generated and purchased power to serve "direct loads," including a number of end use irrigators. *Pacific Gas & Elec. Co.*, 20 F.E.R.C. ¶ 61,190, at 61,366, *order on reh'g and clarification*, 21 F.E.R.C. ¶ 61,115 (1982).[83]

---

[82] The Commission accepted NIMO FERC Rate Schedule 165 in 1990 (permitting it to become effective as of 1987). *Niagara Mohawk Power Corp.*, 51 F.E.R.C. ¶ 61,273, at 61,861 (1990).

[83] *See also Pacific Gas & Elec. Co.*, 50 F.E.R.C. ¶ 61,383, at 62,173 (1990) (discussing PG&E transmission service under Contract 2948A to transport "electricity required to operate [the water storage district's] pumps," *i.e.*, end use customer).

FERC's exercise of jurisdiction over unbundled retail transmission service is not new. What is new is the amount of such service with the introduction of retail choice, and the implications of federal or state jurisdiction over the suddenly expanded use of this interstate transmission service.

B. FERC Cannot Be Faulted For Responding Promptly To The New Market Development of Retail Electric Competition

Order 888 was pro-active in asserting jurisdiction over transmission for unbundled retail customers. When Order 888 issued in April 1996, retail competition (and attendant transmission unbundling) was largely a matter of discussion, and some limited pilot programs. California, the first state to do so, embarked upon retail restructuring and electric competition, on September 23, 1996.[84] FERC understood that it was being pro-active in responding to new market developments likely to arise as a result of increasing competitive market pressures. FERC cogently explained that it was not "taking away" anything from the states and that "[r]ather than claiming 'new' jurisdiction; the Commission is applying the same statutory framework to a business environment in which, as discussed below, retail sales and transmission service are provided in separate transactions." Order 888-A, 62 Fed. Reg. at 12,369, Enron App. E at 476a-477a. FERC found:

> [I]n today's markets, and increasingly in the future as more states adopt retail wheeling programs, retail transactions are being broken into products that are being sold separately: transmission and generation. Moreover, these products are being sold increasingly by two or more different entities. For example, a transaction may involve transmission service from one or more transmission providers who

---

[84] A.B. 1890, 1996 Leg., Reg. Sess. (Cal. 1996) (enacted).

> move power from a distant generation supplier, over the interstate transmission grid, to an end user. Because these types of products and transactions were not prevalent in the past ... the Commission cannot be viewed as "disturbing" the jurisdiction of state regulators ....

Id.

Rather than leaving a jurisdictional void, FERC created the regulatory structure over unbundled retail transmission that has permitted retail choice to go forward. Stimulated by EPAct's intent to promote competitive electricity markets, FERC only "began to address the problem of the disparity in transmission service that utilities provided to third parties in comparison to their own uses of the transmission system" in "the Spring of 1994." Order 888, 61 Fed. Reg. at 21,547, Enron App. D at 159a. Having turned its attention to the problem of discrimination in interstate transmission service supporting competitive electricity markets, FERC swiftly moved to a scheme of uniform open access transmission service. It would have been patently incongruous with the FPA's broad grant of authority over interstate transmission and its directive to remedy undue discrimination for FERC to have declined jurisdiction over the unbundled transmission service used by retail customers to access the competitive interstate market, and instead permitted the balkanization that California openly champions, and New York, by its position, encourages.[85]

[85] New York is correct that industry developments subsequent to the enactment of the statute cannot change the FPA's grant of jurisdiction to FERC (NY Br. at 15), but this does not support New York's position. *Colton*, 376 U.S. at 207 n.1, shows that even where the states have erroneously regulated in a given area for decades, this conduct cannot serve to oust the Commission from exercising its FPA jurisdiction. The FPA grants FERC, and not the states, jurisdiction over public utilities' transmission of electric energy in interstate commerce.

C. The States' Policy Arguments Cannot Eliminate the Need for Federal Regulation of the Interstate Transmission Required for Retail Choice Programs

New York decries Order 888 as unduly disruptive of state retail rate regulation. (NY Br. at 46-48.) California contends that Order 888 "constrain[s]" its efforts to remedy "the electric utility disaster caused by retail restructuring." (CA Br. at 1.) But it was, and is, a state's decision whether to adopt retail competition and implement unbundling. A state that moves to retail competition is substituting market forces for traditional rate regulation of generation costs. The California "disaster" is not caused by FERC's regulation of transmission service; rather, the causes of high market prices include a serious shortage of new generating capacity, a matter which has thus far been left exclusively to the states. Restricting access to generation markets by means of state regulation of interstate transmission is not a formula for lowering energy prices. To the contrary, it is a prescription for capital flight and market avoidance. The States fail to and cannot explain how state control over interstate transmission service is "sound energy policy." (NY Br. at 46.)

Order 888 does what states cannot do on their own. It facilitates retail customer access to interstate electric markets. Unbundled transmission service is provided under the *pro forma* tariff, allowing retail customers to deal with competitive generation suppliers beyond the boundaries of their former supplier and state.

The gap between what states cannot do on their own and what FERC can do and is doing to provide the non-discriminatory open access transmission necessary for competitive generation markets widens into an enormous gulf in the context of independent system operators or regional transmission organizations. This movement toward

regionalization of the transmission grid is required by some state restructuring laws and encouraged by FERC.[86]

Regional transmission organizations take FERC's open access tariffs the next step. They provide retail choice customers, as well as wholesale customers, access to suppliers near and far (even several states removed) under a single regional open access tariff. As recognized by FERC,[87] regional tariffs enhance competition by eliminating the cumulative utility-specific transmission charges otherwise imposed as transactions cross corporate transmission boundaries. Such "pancaked" charges operate as tolls, increasing the cost of energy and constricting the market. Applying a single access charge over a multi-utility region expands competitive power supply options. For example, as a result of an agreement involving two regional organizations, retail choice and wholesale customers in Virginia or Michigan will be able to purchase from generators in Minnesota, Kentucky or Missouri (and most places in between) at a single, "mega-regional" access charge.[88] The scope of the competitive interstate market that retail choice customers can reach through FERC's non-discriminatory open access transmission service continues to grow, further outstripping an individual state's ability to regulate the transmission needed to access that market.

---

[86] *See supra*, at 10 & n.32-34. *See also Regional Transmission Organizations*, Order No. 2000, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,089, 65 Fed. Reg. at 810 (Jan. 6, 2000), *order on reh'g*, Order No. 2000-A, [1996-2000 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,092, 65 Fed. Reg. at 12,088 (Mar. 8, 2000), *appeal docketed sub nom. Pub. Util. Dist. 1 v. FERC*, No. 00-1174 (D.C. Cir. Apr. 24, 2000). FERC found that regional transmission organizations also facilitate efficient and reliable transmission, and eliminate the incentive and opportunity for discrimination. *Id.*

[87] Order No. 2000, 65 Fed. Reg. at 823-25.

[88] *Illinois Power Co.*, 95 F.E.R.C. ¶ 61,183, 2001 FERC LEXIS 1018 (May 8, 2001).

Thus, what is at stake here is not "proper depreciation charges." (NY Br. at 47.) It is, instead, nothing less than the regulatory underpinnings necessary for viable and competitive interstate generation markets.

CONCLUSION

For the reasons indicated above, New York's challenge to the D.C. Circuit's affirmance of FERC Orders 888 and 888-A should be rejected.

Respectfully submitted,

ROBERT C. MCDIARMID
Counsel of Record
CYNTHIA S. BOGORAD
PETER J. HOPKINS
SPIEGEL & MCDIARMID
1350 New York Avenue, NW
Washington, D.C. 20005
(202) 879-4000

Counsel for Respondent Transmission Access Policy Study Group

May 31, 2001

Supreme Court, U.S.
FILED
MAY 10 2001
MAY 10 2001
CLERK

(15) (14)

Nos. 00-568 and 00-809

In The

Supreme Court of the United States

People of the State of New York and the Public Service Commission of the State of New York, et al.
Petitioners,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

Enron Power Marketing, Inc.,
Petitioner,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF FOR THE STATE PUBLIC SERVICE COMMISSIONS AS RESPONDENTS ON THE MERITS IN 00-809

Lawrence G. Malone *
General Counsel
Jonathan D. Feinberg
Carl F. Patka
Diane T. Dean
Assistant Counsel
Public Service Commission
of the State of New York
Three Empire State Plaza
Albany, New York 12223-1350
(518) 474-2510

* Counsel of Record

BECKER GALLAGHER LEGAL PUBLISHING, INC.
CINCINNATI, OH 800-890-5001

48 pp

BEST AVAILABLE COPY

QUESTION PRESENTED IN NO. 00-809

Whether the District of Columbia Circuit correctly affirmed a Federal Energy Regulatory Commission (FERC) decision that it lacked jurisdiction under the Federal Power Act (FPA) subchapter 2, 16 U.S.C. §§ 824, et seq., to regulate the transmission of electric energy "bundled" (i.e., combined) with retail electricity?

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

TABLE OF AUTHORITIES v

PRELIMINARY STATEMENT 1

A. Enactment of the Federal Power Act 1

B. FERC's Decision 3

C. The D.C. Circuit's Decision 3

SUMMARY OF ARGUMENT 4

POINT I 5

THE 1935 CONGRESS DID NOT TRANSFER JURISDICTION OVER RETAIL TRANSMISSION SERVICE FROM THE STATES TO FERC 5

A. The Federal Power Act And Its Legislative History Rebuff Enron's Claim That The 1935 Congress Intended To Prevent State Regulation Of Retail Transmission 5

1. The FPA's Language Defeats Enron's Contention That FERC Has Had Jurisdiction Over All Retail Transmissions Since 1935 5

2. The FPA's Legislative History Demonstrates That Congress Preserved State Jurisdiction Over All Retail Deliveries 7

3. All Relevant FPA Case Law Refutes Enron's Position 12

B. Enron's Reliance On NGA Case Law Is Misplaced 14

C. Enron's Contentions That FERC Has Violated Section 206 By Not Preempting State Regulation Of Retail Transmission Service And Created A Regulatory Gap Are Misplaced 17

1. Section 206 Was Not Intended To Authorize, Much Less Require, FERC Preemption Of Retail Transmission Service 17

2. Enron's Claims Of A Regulatory Gap Are Baseless 18

POINT II 24

ENRON'S CLAIM THAT ALL TRANSMISSIONS ON THE INTERCONNECTED GRID ARE IN INTERSTATE COMMERCE IS IRRELEVANT AND, IN ANY EVENT, INCORRECT 24

A. The Interrelationship Of Transactions On The Grid Does Not Render Retail Transmissions Interstate 25

B. Interconnections Since 1935 Are Not Relevant To The States' Jurisdiction Over Retail Transmissions 26

C. The 1935 Report Further Supports State Jurisdiction Over Retail Transmission Service 27

D. The Case Law Cited By Enron Does Not Support Its Position That All Transmissions Are Interstate 27

CONCLUSION 29

TABLE OF AUTHORITIES

Page(s)

CASES

Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375 (1983) 13, 18, 26

Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) 15

California v. ARC America Corp., 490 U.S. 93 (1989) 20

Connecticut Light & Power Co. v. Federal Power Comm'n, 324 U.S. 515 (1945) 22

Matter of Energy Association of New York v. Public Serv. Comm'n of the State of New York, 169 Misc. 2d 924, 653 N.Y.S. 2d 502 (Albany County 1996) 20

Federal Energy Regulatory Comm'n v. Mississippi, 456 U.S. 742 (1982) 22

Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205 (1964) 12-13

Federal Power Comm'n v. Conway Corp., 426 U.S. 271 (1976) 14

Federal Power Comm'n v. Florida
Power & Light Co.,
404 U.S. 453 (1972) 27-28

Federal Power Comm'n v. Louisiana
Power & Light Co.,
406 U.S. 621 (1972) 12, 15-16

Federal Power Comm'n v. Sierra Power Co.,
350 U.S. 348 (1956) 15

General Motors Corporation v. Tracy,
519 U.S. 278 (1997) 6

Jersey Central Power & Light Co. v.
Federal Power Comm'n,
319 U.S. 61 (1943) 10, 24

Louisiana Public Service Comm'n v.
Federal Communications Comm'n,
476 U.S. 355 (1986) 9

Nantahala Power & Light Co. v. Thornburg,
476 U.S. 953 (1986) 14, 18

New York ex rel. Woodhaven Gas Light Co. v.
Public Serv. Comm'n,
269 U.S. 244 (1925) 20

Northern States Power Co. v. Federal
Energy Regulatory Comm'n,
30 F.3d 177 (D.C. Cir. 1994) 28

Northern States Power Co. v. Federal
Energy Regulatory Comm'n,
176 F.3d 1090 (8th Cir. 1999),
rehearing denied, 1999 U.S. App.
LEXIS 23493 (8th Cir. 1999),
cert. denied sub nom, Enron Power
Marketing Inc. v. Northern States
Power Co., 528 U.S. 1182 (2000) 5, 12

Pennsylvania Gas Co. v. Public Serv.Comm'n,
Second District of the State of New York,
252 U.S. 23 (1920) 27

Public Utilities Comm'n v. Attleboro
Steam & Elec. Co.,
273 U.S. 83 (1927) . . . . . *passim*

Rochester Gas & Electric Corporation v.
Public Service Commission of the
State of New York,
754 F.2d 99 (2d Cir. 1985) 18

Transmission Access Policy Study Group v.
Federal Energy Regulatory Comm'n,
225 F.2d 667 (D.C. Cir. 2000) 3

United States v. Public Utilities Comm'n
of California,
345 U.S. 295 (1953) 13

Younger v. Jensen,
26 Cal.3d 397, 605 P.2d 813 (1980) 21

FEDERAL STATUTES

FPA §§ 201(a)[16 U.S.C. § 824(a)] . . . . . *passim*

FPA § 201(b)[16 U.S.C. § 824(b)] 8, 9, 15

FPA § 201(c)[16 U.S.C. § 824(c)] 24, 29

FPA § 201(e)[16 U.S.C. § 824(e)] 24

FPA § 205[16 U.S.C. § 824d] 6, 12

FPA § 206(a)[16 U.S.C. § 824e(a)] 17

FPA § 206(d)[16 U.S.C. § 824e(b)] 6, 17

FPA § 212(h)[16 U.S.C. § 824j(h)] 2

FPA § 212(h)[16 U.S.C. § 824k(h)] 1, 2, 6, 7, 14

FPA § 212(h)[16 U.S.C. § 824l(h) 2

FPA § 212(h)[16 U.S.C. § 824m(h)] 2

47 U.S.C. § 220 9

STATE STATUTES

Idaho Code Section 61-315 19

New York General Business Law § 340 et seq. 20

New York Public Service Law § 2(13) 20

New York Public Service Law § 4(1) 19

New York Public Service Law § 65(1) 19

New York Public Service Law § 66(1) 19

New York Public Service Law § 65(3) 20

New York Public Service Law § 66(6) 19

New York Public Service Law § 72 19

NGA § 1(c), 15 U.S.C. § 717(c) 15

NGA § 7f(2), 15 U.S.C. § 717f(2) 15

LEGISLATIVE HISTORY

Solicitor DeVane, Analysis of Wheeler Bill, S. 1725, pp. 104 to 140, Regulation of Interstate Commerce in Electric Energy, Hearings on S. 1725 Before the House Committee on Interstate and Foreign Commerce, 74th Congress (1935) 6

House Comm. on Energy and Commerce, Energy Policy Act of 1992, P.L. 102-486, House Report No. 102-474(I) at 138, 140 (1992), reprinted in 1992 U.S.C.C.A.N. 1953, 1963 . . . . . 2, 7

H.R. Rep. No. 74-1318 (1935) 6-11

Memorandum of Oswald Ryan and Dozier DeVane in Public Utility Holding Co. Act of 1935; Hearings on S. 1725 Before the Senate Committee on Interstate Commerce 74th Cong. (1935) 26

Public Utility Holding Co. Act of 1935, Hearings on S. 1725 Before the Senate Committee on Interstate Commerce, 74th Cong. (1935) . . . . . *passim*

ADMINISTRATIVE
CASES AND MANUALS

Applicability of Common Carrier Concept to Modern Telecommunications; Case 89-C-099; Opinion No. 90-9, Opinion and Order Adopting Regulations Concerning Common Carriage, New York Public Service Commission, 1990 N.Y. PUC LEXIS 4; 110 P.U.R. 4th 107 (issued February 20, 1990) 20

Case 96-E-0909, Central Hudson Gas & Electric Corporation - Plans for Electric Rates and Restructuring - Order Authorizing the Process for the Auctioning of Generation Plan and Modifying Prior Orders, 2000 N.Y. PUC LEXIS 93 (issued February 23, 2000) 21

Competitive Opportunities Regarding Electric Service, Case 94-E-0952, New York Public Service Commission, Order Providing for Competitive Metering, 1999 N.Y. PUC LEXIS 280, 194 P.U.R. 4th 129 (issued June 16, 1999) 23

In the Matter of Competitive Opportunities Regarding Electric Service, Case 94-E-0952; Opinion No. 97-13, Opinion and Order Establishing Regulatory Policies for Competitive Metering, New York Public Service Commission, 1997 N.Y. PUC LEXIS 450, 181 P.U.R. 4th 324 (issued August 1, 1997) 23

Re Competitive Opportunities Regarding Electric Service, Cases 94-E-0952 et al.; Opinion No. 96-12, Opinion and Order Regarding Competitive Opportunities for Electric Service, New York Public Service Commission, 1996 N.Y. PUC LEXIS 330, 168 P.U.R. 4th 515 (issued May 20, 1996) 23

Case 96-E-0897, Consolidated Edison Company of New York. - Plans for Electric Rates and Restructuring, Order Authorizing the Process for the Auctioning of Generation Plant, 1998 N.Y. PUC LEXIS 414, 188 P.U.R. 4th 149 21

Customer Billing Arrangements Alternative Billing Arrangements, Case 99-M-0631, New York Public Service Commission, Order Providing for Customer Choice of Billing Entity, 2000 N.Y. PUC LEXIS 283, 200 P.U.R. 4th 149 (issued March 22, 2000) 23

Electronic Data Interchange, Case 98-M-0667; Opinion No. 00-05, Opinion and Order on Implementation of Electronic Data Interexchange, New York Public Service Commission, 2000 N.Y. PUC LEXIS 411, 200 P.U.R. 4th 329 (April 12, 2000) 23

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and transmitting Utilities, Order No. 888 [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ at 31, 036, 61 Fed. Reg 21, 540 (1996), ("FERC Order 888") at 31, 643-44 2

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Standard Costs by Transmitting Utilities, Order No. 888-A [Reg. Preambles] III F.E.R.C. Stats. & Regs. ¶ 31, 048, 62 Fed Reg. 12, 274 (1997), ("FERC Order 888-A") at 30, 225-226 3

Issues Related to the Continuing Provision of Universal Service and to Develop a Regulatory Framework for the Transition to Competition in the Local Exchange Market, Case 94-C-0095; Opinion No. 96-13 Opinion and Order Adopting Regulatory Framework, New York Public Service Commission, 1996 N.Y. PUC LEXIS 270 [A 39]; 171 P.U.R. 4th 30, 43 (issued May 22, 1996) 20

Case 96-E-0891, New York State Electric & Gas Corporation - Plans for Electric Rates and Restructuring, Order Authorizing the Process for the Auctioning of Generation Plant (1998 N.Y. PUC LEXIS 192 (issued April 24, 1998) 21

Cases 94-E-0098 and 94-E-0099, Niagara Mohawk Power Corporation - PowerChoice Rate and Restructuring Plan, Order Authorizing Process for the Auctioning of Generating Facilities, 1998 N.Y. PUC LEXIS 259 (issued May 6, 1998) 21

Case 96-E-0900, Orange and Rockland Utilities, Inc. - Plans for Electric Rates and Restructuring, Order Authorizing the Process for the Auctioning of Generation Plant and Rejecting Joint Agreement, 1998 N.Y. PUC LEXIS 259 (issued April 16, 1998); 1998 N.Y. PUC LEXIS 374 21-22

Cases 96-E-0900, 94-E-0098, 94-E-0099, 96-E-0891, 96-E-0897, 96-E-0909, 96-E-0898 - Orange & Rockland Utilities, Inc., Niagara Mohawk Power Corporation, New York State Electric & Gas Corporation, Consolidated Edison Company of New York Inc., Central Hudson Gas & Electric Corporation, Rochester Gas and Electric Corporation - Plans for Electric Rate Restructuring, Statement of Policy Regarding Vertical Market Power [encouraging divestiture], 1988 N.Y. PUC LEXIS 432; 187 P.U.R. 4th 223 (July 17, 1998) 21

Matter of Retail Access Business Rules, Case 98-M-1343; Opinion No. 99-3, Opinion and Order Concerning Uniform Business Practices, New York Public Service Commission, 1999 N.Y. PUC LEXIS 28, 190 P.U.R. 4th 369 (issued February 16, 1999), rehearing granted in part, 1999 N.Y. PUC LEXIS 95 (issued April 15, 1999) 23

OTHER MATERIALS

Reply Brief in Support of Petition for Certiorari Enron Power Marketing Inc. v. Northern States Power Co., Supreme Court No. 99-916 12-13

Electric Power Research Institute (EPRI), A Primer on Electric Power Flow for Economists and Utility Planners (1995) 25

B.M. Weedy, B.J. Cory, Electric Power Systems (1998) 26

R. Sarikas, Introduction to Electrical Theory and Power Transmission (1995) 25

PRELIMINARY STATEMENT

Enron[1] challenges FERC's[2] conclusion that FERC lacks jurisdiction to regulate bundled retail transmission service. In effect, it claims that FERC has misread the FPA since its enactment in 1935.

Enron's position is baseless. The 1935 Congress denied FERC jurisdiction of all elements of retail service (FPA § 201), which included the delivery of energy. Public Utility Holding Companies, Hearings on H.R. 5423 before the House Committee on Interstate and Foreign Commerce, testimony of FERC Solicitor DeVane ("DeVane") at 556. The 1992 Congress, in enacting FPA § 212(h) (discussed below) reaffirmed state jurisdiction over retail transmission and left decisions on whether to allow retail competition to the states.

A. Enactment Of The Federal Power Act

In 1935, Congress passed the FPA. Its purpose was to fill a jurisdictional gap created by a Supreme Court decision barring states from regulating rates of wholesale energy sold across state lines. Public Utilities Comm'n of Rhode Island v. Attleboro Steam and Electric Co., 273 U.S. 83, 89 (1927). Because, with the absence of state regulation, there was no regulation of interstate sales, Congress filled this

---

[1] "Enron" refers to Enron Power Marketing, Inc., petitioner in 00-809. Enron is supported by the Electric Power Supply Association (EPSA) and Electricity Consumers Research Council (ECRC), which essentially repeat Enron's arguments.

[2] The Federal Energy Regulatory Commission and its predecessor, the Federal Power Commission, will be referred to as "FERC."

"Attleboro gap" by empowering FERC to regulate wholesale electricity rates. Congress, however, preserved the states' regulation over retail matters by providing that "Federal regulation is to extend only to those matters which are not subject to regulation by the States" (emphasis added) (§ 201(a)).

Beginning in the late 1970's, new entrants into the generation market sought access to transmission lines in order to make bulk sales. Joint Appendix ("J.A.") 74-77, Enron Appendix ("App.") 152a-154a, Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888 [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996), ("FERC Order 888") at 31,643-44. Congress eventually responded in the Energy Policy Act of 1992 (EPAct) by giving FERC greater authority to require transmission owners to provide transmission service to power suppliers competing with utilities. 16 U.S.C. §§ 824j-824m.

While the statute clarified FERC's authority to order utilities to provide wholesale transmission service, it also "prohibited FERC from forcing utilities to engage in 'retail wheeling,' the transmission of power directly to a retail customer." House Comm. on Energy and Commerce, Energy Policy Act of 1992, P.L. 102-486, House Report No. 102-474(I) at 140 (1992), reprinted in 1992 U.S.C.C.A.N. 1953, 1963. Thus, it directed that "[n]othing in this subsection [§ 212(h)] shall affect any authority of any State or local government under state law concerning the transmission of electric energy directly to an ultimate consumer."

B. FERC's Decision

In the decision under review, FERC decided open access to transmission was necessary to advance competition in the wholesale power market. J.A. 48, Enron App. 131a, FERC Order 888 at 31,634. In addition to requiring wholesale open access, FERC preempted the states' jurisdiction of retail transmission when states "unbundle" the commodity from delivery (presumably to implement retail competition). It, however, recognized traditional state control over bundled retail transactions.

Thus, in Order 888, FERC adhered to established practice with respect to bundled service and acknowledged that Congress did not alter state regulation of all aspects of bundled retail service. J.A. 349-50, Enron App. 306a, FERC Order 888 at 31,781. On rehearing, FERC adhered to its position that it would not attempt to unbundle retail service. Enron App. 455a, Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Standard Costs by Transmitting Utilities, Order No. 888-A [Reg. Preambles] III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997), ("FERC Order 888-A") at 30,225-226, citing FERC Order 888 at 31,781, J.A. 349-50.

C. The D.C. Circuit's Decision

On June 30, 2000, a Panel of the D.C. Circuit upheld FERC's decision not to preempt state regulation of bundled retail transmission service. Transmission Access Policy Study Group v. Federal Energy Regulatory Comm'n, 225 F.2d 667, 692-95 (D.C. Cir. 2000).

SUMMARY OF ARGUMENT

The State Petitioners' brief on the merits demonstrated that FERC Order 888 erred in assuming that the 1935 Congress: (1) failed to safeguard state regulation of the transmission portion of retail deliveries; (2) assigned FERC jurisdiction of unbundled retail transmissions in interstate commerce; and (3) provided that all retail transmissions on the interconnected grid would be in interstate commerce (State Petitioners at 10). Point I of Enron's brief combines (and expands) FERC's first two premises by contending that the 1935 Congress not only failed to deny FERC jurisdiction over matters regulated by the states, but removed jurisdiction of even bundled retail transmission jurisdiction from the states and gave it to FERC (Enron Brief as Petitioners in 00-809, hereafter "Enron" at 21-24). Enron's Point I -- that the 1935 Act preempted state regulation of retail transmission in interstate commerce -- is answered in Point I, below.

The second Point of Enron's brief claims that all retail transmissions on the interconnected grid are in interstate commerce (Enron at 27-33).[3] Point II below addresses Point II of Enron's brief.

---

[3] This part of Enron's brief echoes FERC's third premise.

POINT I

THE 1935 CONGRESS DID NOT TRANSFER JURISDICTION OVER RETAIL TRANSMISSION SERVICE FROM THE STATES TO FERC

A. The Federal Power Act And Its Legislative History Rebuff Enron's Claim That The 1935 Congress Intended To Prevent State Regulation Of Retail Transmission

1. The FPA's Language Defeats Enron's Contention That FERC Has Had Jurisdiction Over All Retail Transmissions Since 1935

Enron's argument for FERC jurisdiction over transmissions in bundled retail rates ignores the FPA's goal of limiting federal regulation "to those matters which are not subject to regulation by the States." FPA § 201(a) [16 U.S.C. § 824(a)]. In giving FERC authority over matters the states could not regulate, Congress protected the states' jurisdiction over matters they could regulate, specifically retail transactions.

Neither Attleboro nor any other case law has even remotely suggested that state regulation of bundled retail transactions runs afoul of the Commerce Clause. To the contrary, Northern States Power Co. v. Federal Energy Regulatory Comm'n, 176 F.3d 1090, 1096 (8th Cir. 1999), rehearing denied, 1999 U.S. App. LEXIS 23493 (8th Cir. 1999), cert. denied sub nom., Enron Power Marketing v. Northern States Power Co., 528 U.S. 1182 (2000), held that FERC's "attempt to regulate the curtailment of electrical

transmission on native/retail consumers is unlawful, because it falls outside of the FPA's specific grant of authority to FERC." See General Motors Corporation v. Tracy, 519 U.S. 278, 294 (1997) [state can distinguish between bundled utility service and unbundled supply of gas in levying taxes].

As indicated in the State Petitioners' brief on the merits in Case 00-568 (at 27-28), Section 201(a) provides that "Federal regulation [is] . . . to extend only to those matters which are not subject to regulation by the States." Section 205 limits FERC's transmission authority by stating that it may set the rates for transmission "subject to the jurisdiction of the Commission. . . ." (emphasis added). Section 206(d) implicitly recognizes the states' jurisdiction over retail transmission by contrasting FERC's broad jurisdiction over transmission facilities with its lack of jurisdiction over retail service and calling on FERC to provide costs to states in order to facilitate state regulation of retail transmission service. See H.R. Rep. No. 74-1318, at 8 (bill takes no authority from States and authorizes FERC "to aid the State commissions in their efforts to ascertain and fix reasonable charges").[4]

---

[4] Public Utility Holding Company Act of 1935, Hearings Before the Senate Committee on Interstate Commerce on S. 1725, 74th Cong. (1935) ("1935 Hearings on S. 1725") at 245, 247 (Memorandum of FERC Solicitor DeVane, "Analysis of Wheeler Bill, S. 1725, pp. 104 to 140") ["It cannot be too strongly emphasized that the ratemaking power conferred on the Commission by Sections 207 and 208 is limited to the field in which States have no constitutional authority. Under the provisions of this title, the power of the States to regulate retail distribution rates, even where the energy comes directly from another State is expressly preserved; wholesale rates alone are made the subject of the Commission's jurisdiction"].

Enron's position also flies in the face of EPAct. FPA § 212(h) [16 U.S.C. § 824k(h)] provides that "[n]othing in this subsection shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an ultimate consumer."[5] If, as Enron claims, Congress meant to give FERC jurisdiction over all transmission, it would not have reserved to the states decisions on whether to allow transmissions directly to retail customers. Moreover, it would not have denied FERC authority to require unbundling of retail transactions.[6]

2. The FPA's Legislative History Demonstrates That Congress Preserved State Jurisdiction Over All Retail Deliveries

The legislative history of the 1935 Act evidences Congress' goal of filling the Attleboro gap, which prevented states from regulating wholesale electricity sales in interstate commerce while -- at the same time -- preserving state regulation of retail electric service, including retail transmissions (State Petitioners' Br. at 18-26). In claiming

---

[5] Section 212(h)'s legislative history states that "[t]he bill's electricity provisions will promote additional competition in wholesale electricity power market in order to improve the efficiency of the electric utility industry and secure the lowest possible costs for consumers" (emphasis added). Energy Policy Act of 1992, P.L. 102-486, House Report No. 102-474(I) at 138 (1992), reprinted in 1992 U.S.C.C.A.N. 1953, 1961.

[6] Section 212(h) states "no order issued under this chapter shall be conditioned upon or require the transmission of electric energy: (1) directly to an ultimate consumer, or (2) to or for the benefit of an entity if such electric energy would be sold by such entity directly to an ultimate consumer . . ." [16 U.S.C. § 824k(h)].

that Congress intended to grant FERC plenary authority over retail transmissions in interstate commerce, Enron has selected four items from the legislative record, none of which support its theory (Enron at 23-25).

First, Enron cites the Senate Report on Section 201, which stated "[j]urisdiction is asserted ... over all interstate transmission lines whether or not there is a sale of the energy carried by those lines . . . ." (Enron at 23; quoting S. Rep. No. 74-621, at 48 (1935)). Immediately preceding the quoted language, however, the Senate Committee on Interstate Commerce stated that Section 201(b)

> leaves to the States the authority to fix local rates even in cases where the energy is brought in from another State. . . . The present bill carefully refrains from asserting Federal jurisdiction over these rates. The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in Public Utilities Commission v. Attleboro Steam & Electric Co. (271 U.S. 83), to be beyond the reach of the States.

S. Rep. No. 74-621, at 48 (1935). Thus, Section 201(b) does not authorize FERC to regulate retail transmissions.

Second, Enron argues that Congress' failure to adopt an amendment to Section 201(b), offered by the National Association of Railroad and Utility Commissioners (NARUC), that would have limited federal jurisdiction "to the transmission and sale at wholesale of electric energy in interstate commerce," suggests that Congress intended FERC to regulate all transmission service (Enron at 23). Enron's

position is similar to that of a respondent-intervenor in Louisiana Public Service Comm'n v. Federal Communications Comm'n (FCC), 476 U.S. 355, 377 (1986), wherein GTE contended that Congress' rejection of anti-preemption language in the Communication Act's depreciation provision (47 U.S.C. § 220) demonstrated Congress' intent to allow FCC preemption of local depreciation charges. Just as GTE's argument ignored Congress' enactment of Section 152(b) of the Communications Act, which preserved state jurisdiction over intra-state telecommunication matters, Enron's contention ignores Congress' enactment of Section 201(a) of the FPA, which preserved pre-existing state regulation over retail matters.

In negotiating the 1935 FPA, as well as the 1934 Communications Act, the states were not wedded to particular language. Their sine qua non for the FPA was that the statute preserve pre-existing state jurisdiction. Thus, on the same day that NARUC offered its version of Section 201(b) it also successfully urged Congress to amend Section 201(a) to provide that "nothing contained in this title shall be construed to extend Federal regulation to that part of said business which is subject to regulation by the States."[7] See Public Utility Holding Cos. Hearings before House Committee on Interstate and Foreign Commerce on H.R. 5423 ("1935 Hearings on H.R. 5423"), 74th Congress (1935) (statement of

---

[7] Section 201(a), as enacted, allows "such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States." 16 U.S.C. § 824(a). Mr. Benton stated that such language should "be incorporated as a clear declaration by Congress of its intent to grant the power to the Federal body to regulate that which is beyond the jurisdiction of the local commission" (emphasis added). 1935 Hearings on H.R. 5423 at 1677.

John E. Benton, General Solicitor of NARUC), at 1660. Because the states regulated retail transmission in 1935, preserving pre-existing state regulation would safeguard state regulation of retail transmissions. See Benton, 1935 Hearings on S. 1725 at 767-68, 1935 Hearings on H.R. 5423 at 1657; DeVane, 1935 Hearings on H.R. 5423 at 498 ["The theory upon which the bill is drawn is that the consumer's rate is left to regulation by state commissions."]

Congress accepted § 201(a) and thereby preserved pre-existing state regulation "even in those cases where the energy is brought in from another State" (H.R. Rep. No. 74-1318 at 27 (1935)). Although FERC opposed NARUC's original version of § 201(b) limiting federal jurisdiction to those utilities that transacted the majority of their business in interstate commerce (because it could have impeded FERC's ability to facilitate interconnections) (DeVane, 1935 Hearings on H.R. 5423 at 2144-2149), it supported § 201(a), acknowledging that Section 201(a) limited FERC's rate jurisdiction to wholesale transactions in interstate commerce (DeVane, 1935 Hearings on H.R. 5423 at 497-498, 518) and noted that it did not wish to regulate retail matters.[8] The states, in turn, supported the FPA because Section 201(a), among other things, safeguarded their jurisdiction over all elements of retail service. See Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61, 74 (1943) [§ 201(a) preserves state regulation over "generation, transmission and sales" to retail customers] (emphasis added).

Enron's third selection of legislative history is a statement by Mr. Arkwright, the then-President of Georgia

---

[8] DeVane, 1935 Hearings on H.R. 5423 at 2143, 2144, 2146, 2154.

Power Company. Mr. Arkwright stated that "[w]hether it be wholesale or retail, as I understand it, the transmission of the current from one State to another is interstate commerce" (Enron 23-24). 1935 Hearings on H.R. 5423 (statement of John Preston Arkwright), at 661. He then went on, however, to offer his opinion that:

> electric current distributed is subject exclusively to the jurisdiction of the State for regulation, no matter where the current came from, whether it had been transmitted across State lines or not.

Id. at 666.

Last, Enron argues that the House and Senate committee reports confirm that FERC's jurisdiction over transmission in interstate commerce should include transmission for bundled retail transactions (Enron at 25). The committee reports confirm the opposite -- that Congress understood that the states would have jurisdiction over retail transmissions.

The House Report states that "the authority of States to fix local rates is not disturbed even in those cases where the energy is brought in from another State." H.R. Rep. No. 74-1318 at 27 (1935). If the House Committee on Interstate and Foreign Commerce had intended to grant FERC jurisdiction over retail transmission, it would not have declared, in the face of the states' then long-standing role in deciding retail electric matters, that "[t]he bill takes no authority from State commissions and contains provisions authorizing the Federal Commission to aid the State commissions in their efforts to ascertain and fix reasonable charges." Id. at 8. Indeed, the Committee mused that "[p]robably, no bill in recent years has

so recognized the responsibilities of State regulatory commissions as does title II of this bill." Id. at 8.

Likewise, the Senate Committee on Interstate Commerce reported that the FPA was designed to fill the gap in the regulation of interstate wholesale sales created by the Attleboro case (S. Rep. No. 74-621, at 17) and to provide FERC jurisdiction over "interstate transmission where there is no sale." Id. at 19. Rather than asserting jurisdiction over retail transmission, the Senate report eschews "every encroachment upon the authority of the States. The revised bill would impose regulation only over those matters which cannot effectively be controlled by the States." Id. at 18.

3. All Relevant FPA Case Law Refutes Enron's Position

Enron and its supporters (ECRC and EPSA) essentially claim that FERC has misread the FPA for more than 65 years. Case law under the FPA indicates otherwise. Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205, 212-15 (1964) [There is a "bright line" between state power over retail transactions and federal power over wholesale transactions].[9]

---

[9] Enron basically reiterates the contentions rejected by the Circuit Court of Appeals in Northern States Power, 176 F.3d at 1090. Specifically, Enron again claims that Federal Power Comm'n v. Louisiana Power & Light, 406 U.S. 621 (1972) supports FERC jurisdiction over bundled retail transmission (Enron at 8, 17, 22-24) and that FERC must regulate the retail transmission element of bundled retail service in order to correct alleged discrimination against wholesale competitors (Enron, 39-43) (Compare Enron Reply Brief In Support of Petition for Certiorari, at 6-7 in Enron Power Marketing Inc. v. Northern States Power Co., Supreme

This Court has emphasized that the purpose of the FPA was to "adopt the test developed in the Attleboro line, which "denied state power to regulate a sale 'at wholesale to local distributing companies' and allowed state regulation of a sale 'at local retail rates to ultimate consumers. (emphasis added)'"; [citation omitted]. FPC v. Southern Cal. Edison Co., 376 U.S. at 214. United States v. Public Utilities Comm'n of California, 345 U.S. 295, 308 (1953) ["Congress interpreted [Attleboro] as prohibiting state control of wholesale rates in interstate commerce for resale, and so armed the Federal Power Commission with precisely that power"].

Enron argues (Enron at 8, n. 8) that the wholesale/retail demarcation of FPC v. Southern California Edison Co. applies only to "sales."[10] FPC v. Southern California Edison and Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375, 380 (1983) held, however, that the wholesale/retail line is a mechanistic dividing line between state and federal jurisdiction.[11]

Court No. 99-916).

[10] By "sales," Enron apparently refers to the provision of energy. A retail transaction involves the provision and sale of the commodity, transmission, distribution, metering and billing service.

[11] FPC v. Southern California Edison Co., 376 U.S. at 215-16 ["Congress meant to draw a bright line easily ascertained between state and federal jurisdiction, making unnecessary such case-by-case analysis"]. Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375, 380 (1983) ["Congress, partly to avoid 'drawing the precise line between federal and state power by the litigation of particular cases' ... had adopted the 'mechanical' line established in Kansas Gas and Attleboro as the statutory line

Further, Enron argues (Enron at 26-27) that the FERC retail transmission price should be an element of the retail rate, citing the holding of Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953, 966 (1986), that a state regulator should recognize a FERC-approved wholesale rate. Nantahala recognized FERC's "exclusive jurisdiction over the rates to be charged Nantahala's interstate wholesale customers" (emphasis added). 476 U.S. at 966. It did not, however, permit FERC to set a bundled retail rate. Rather, Nantahala held that states must recognize FERC wholesale rates, and FERC allocations of wholesale power as costs, in setting retail rates. 476 U.S. at 971.[12]

B. Enron's Reliance On NGA Case Law Is Misplaced

Enron and EPSA reference (Enron at 17, 22, 32; EPSA at 6) case law under the Natural Gas Act (NGA) for the proposition that FERC, not the states, must regulate the transmission component of a bundled retail transaction. Enron claims that the Court has followed an "established practice of citing interchangeably decisions interpreting the

---

dividing federal and state jurisdiction"]. If such a mechanical line is to have its intended benefits of simplifying jurisdictional controversies, it must apply to the statute as a whole.

[12] EPSA argues (EPSA Brief "EPSA" at 12-13) that FPC v. Conway Corp., 426 U.S. 271 (1976), supports FERC power over retail services insofar as that case concluded FERC had jurisdiction to address a "price squeeze" between retail and wholesale rates. Inasmuch as FPC v. Conway Corp. held FERC could not adjust a retail rate, it supports the States' position in this case. 426 U.S. at 276-77. FERC could consider the difference between wholesale and retail rates, but it could only do so in setting the wholesale rate. 426 U.S. at 280.

pertinent sections of the two statutes" (Enron at 22, citing Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571, 577, n. 7 (1981)), but that practice is apparently followed, however, only when the "relevant provisions of the two statutes 'are in all material respects substantially identical (emphasis added).'" 453 U.S. at 577, n. 7, citing Federal Power Comm'n v. Sierra Power Co., 350 U.S. 348, 353 (1956). The Natural Gas Act contains no "relevant" provision similar to FPA Sections 201(a) or 212(h).

Enron chiefly relies on Federal Power Comm'n v. Louisiana Power & Light Co., 406 U.S. 621 (1972), which held that FERC could curtail interstate transportation of natural gas to industrial customers, although the transportation was occurring in association with non-jurisdictional direct sales of natural gas. 406 U.S. at 640-41. The case is not supportive of Enron's position for several reasons.

First, it did not concern NGA § 1(c), 15 U.S.C. § 717(c), which provides that where a gas buyer and seller are in the same state, FERC does not have jurisdiction over retail deliveries. ["The provisions of this chapter shall not apply to any person engaged in or legally authorized to engage in the transportation in interstate commerce or the sale in interstate commerce for resale, of natural gas received by such person from another person within or at the boundary of a State if all the natural gas so received is ultimately consumed within such State, or to any facilities used by such person for such transportation or sale, provided that the rates and services of such person or facilities be subject to regulation by a State commission"].[13] Second, Federal Power

---

[13] We anticipate Enron will argue that the existence of NGA § 1(c) supports its position because such a provision was not included in

Comm'n v. Louisiana Power & Light did not concern NGA § 7f(2), 15 U.S.C. § 717f(2), which denies FERC jurisdiction over service across state lines to retail consumers if the transportation is in the utility's service territory.[14] ["[T]ransportation to ultimate customers in such service area by the holder of such service area determination, even if across state lines, shall be subject to the exclusive jurisdiction of the State commission in the State in which the gas is consumed"]. Third, as indicated, the NGA does not contain a corollary to either FPA § 201(a) or § 212(h), which-again-deny FERC jurisdiction over retail transmissions.

---

the Federal Power Act. However, such an argument would ignore the fact that FERC had repeatedly argued that the addition of any amendment like NGA § 1(c) to the Federal Power Act was unnecessary because the Federal Power Act adequately protected state authority over retail rates and local services. Amendments to Federal Power Act, Hearings on H.R. 2972 before the House Committee on Interstate and Foreign Commerce, 80th Cong. (1947) at 336 (statement of FERC Chairman Smith) 527, 548, 574-75 (statement of FERC Assistant General Counsel Wahrenbrock). Federal Power Act Amendments of 1967, Hearings on H.R. 5348, H.R. 5637, H.R. 7799, H.R. 8426, H.R. 8919, H.R. 9174 before the Subcommittee on Communications and Power of the House Committee on Interstate and Foreign Commerce, 90th Cong. (1967) at 123-125 (statement of FERC Chairman White).

[14] Electric utilities sell electricity to retail customers in their service territories.

C. Enron's Contentions That FERC Has Violated Section 206 By Not Preempting State Regulation Of Retail Transmission Service And Thereby Created A Regulatory Gap Are Misplaced

Enron and ECRC allege that Section 206 requires FERC to regulate retail transmission service because the States are unable to prevent vertically integrated utilities from providing retail transmission service in a manner that prejudices wholesale competitors (Enron at 31-32, ECRC Brief ("ECRC") at 12-13). Its position misconstrues Congress' intent in enacting Section 206 and ignores the states' demonstrated ability to prevent discriminatory utility behavior.

1. Section 206 Was Not Intended To Authorize, Much Less Require, FERC Preemption Of Retail Transmission Service

Section 206(a) allows FERC, on its own motion, to examine whether utility rates "subject to the jurisdiction of the commission" are discriminatory and, if so, to rectify such discrimination. Subdivision (d) of Section 206 recognizes state authority to set transmission rates and empowers FERC to assist state ratemaking by providing states, upon request, "the cost of the . . . transmission of electric energy by means of facilities under the jurisdiction of the Commission . . . ." Section 206, therefore, authorizes FERC to correct discriminatory wholesale rates and to assist the states in setting retail rates.

2. Enron's Claims Of A Regulatory Gap Are Baseless

Enron, ECRC and EPSA contend that FERC Order 888 allows a vertically integrated utility to discriminate against wholesale competitors by reserving large portions of the interstate grid for bundled retail transactions and leaving wholesale competitors with insufficient capacity (Enron at 41-43, ECRC at 19-20, EPSA at 6-10). Order 888, however, limits the ability of a utility to reserve transmission capacity for native load to levels needed to accommodate reasonable growth. J.A. 291, Enron App. 267a, FERC Order 888 at 31,745. If a utility unreasonably forecasts growth, and thereby foregoes revenue from wholesale customers, regulators may impute the foregone revenue to the utility for retail ratemaking purposes, leaving utility management answerable to shareholders. See Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953, 972 (1986) ["Without deciding this issue, we may assume that a particular quantity of power provided by a utility from a particular source could be deemed unreasonably excessive [by a state commission] if lower cost power is available elsewhere . . ."]; Rochester Gas & Electric Corporation v. Public Service Comm'n of the State of New York, 754 F.2d 99 (2d Cir. 1985) [upholding NYPSC imputation of incidental revenues from wholesale sales].

Enron's and EPSA's allegation that state commissions are unable to eliminate undue discrimination (Enron at 44, EPSA at 10) is also incorrect.[15] State regulators are

[15] Arkansas Electric Cooperative Corp. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375, 377, 384 (1983) does not support Enron's argument that the FPA leaves a regulatory gap (Enron at 32-33).

authorized to (1) assure that retail transmission rates are "just and reasonable" (e.g., New York Public Service Law [NYPSL] § 65(1); (2) require utilities to provide services in a non-discriminatory manner (NYPSL § 65(3)); see also Idaho Code Section 61-315; (3) prescribe corrective behavior if a utility acts in "anywise in violation of any provision of law" (NYPSL § 66(6)); and (4) "order such improvement in the. . . transmission of electricity or in the methods employed by such person or corporation, as will in its judgment be adequate, just and reasonable" (NYPSL § 72).[16] Indeed, state regulatory agencies normally have "general supervision of all . . . electric corporations" and "all electric plants" and "all powers necessary or proper to enable it to carry out the purposes of" the Public Service Law (e.g., NYPSL §§ 66(1); 4(1)).

State law prohibits utilities from granting "an undue preference or advantage to any person, corporation or locality, or to any particular description of service (emphasis

In that case, the Court relied on the fact that retail utilities receive out of state power, "and the national fabric does not seem to have been seriously disturbed by leaving regulation of retail utility rates largely to the states." 461 U.S. at 395. Here, of course, Enron is trying to limit state regulation of the very out-of-state transmission of energy on which the Court relied as a basis for its decision in Arkansas Electric Corp. Enron argues that Arkansas Electric Coop. Corp. shows Congress did not intend to leave the electric industry unregulated (Enron at 32-33, quoting 46 U.S. at 384). The Court relied upon that principle to reject claims like Enron's that states were preempted.

[16] The New York Public Service Law is illustrative of state power to address discrimination. Other states have very similar grants of jurisdiction.

added)"; (e.g., NYPSL § 65(3); New York General Business Law § 340 et seq. (precluding monopolies)). Utilities, therefore, may not grant themselves preferences (NYPSL § 2(13)). See Matter of Energy Ass'n of New York State v. Public Service Commission of the State of New York, 169 Misc. 2d 924, 932-36, 653 N.Y.S. 2d 502, 510-512 (Albany County 1996). See also, Case 94-C-0095, Issues Related to the Continuing Provision of Universal Service and to Develop a Regulatory Framework for the Transition to Competition in the Local Exchange Market, Opinion No. 96-13, Opinion and Order Adopting Regulatory Framework, New York Public Service Commission, 1996 N.Y. PUC LEXIS 270 [A 39]; 171 P.U.R. 4th 30, 43 (issued May 22, 1996) [discussing imputation guidelines for comparing retail and wholesale prices]; Case 89-C-099, Applicability of Common Carrier Concept to Modern Telecommunications; Opinion No. 90-9, Opinion and Order Adopting Regulations Concerning Common Carriage, New York Public Service Commission, 1990 N.Y. PUC LEXIS 4; 110 P.U.R. 4th 107 (issued February 20, 1990).

Additional state commission tools for avoiding anti-competitive utility behavior include conditioning discretionary rates on non-preferential use of utilities' transmission networks and acting on complaints of customers seeking the delivery of competitors' electricity. New York ex rel. Woodhaven Gas Light Co. v. Public Serv. Comm'n, 269 U.S. 244, 248 (1925) [upholding the state's power to require utilities to extend services for legitimate public purposes]; California v. ARC America Corp., 490 U.S. 93, 103 (1989) [rejecting claims that state antitrust laws are preempted by federal law because "[i]t is one thing to consider Congressional policies . . . in defining what sort of recovery federal antitrust law authorizes; it is something altogether different, and in our view inappropriate, to consider them as

defining what federal law allows states to do under their own antitrust law"]. See Younger v. Jensen, 26 Cal. 3d 397, 605 P.2d 813 (1980) [state antitrust investigation against regulated entities].

Rather than simply reacting to claims of discrimination, state commissions have also acted to discourage discriminatory use of retail transmission service. New York State, for example, has removed utility incentives to use the delivery system in a discriminatory manner by inducing the sale of nearly all utility-owned power plants.[17]

---

[17] Cases 96-E-0900, 94-E-0098, 94-E-0099, 96-E-0891, 96-E-0897, 96-E-0909 - Orange & Rockland Utilities, Inc., Niagara Mohawk Power Corporation, New York State Electric & Gas Corporation, Consolidated Edison Company of New York Inc., Central Hudson Gas & Electric Corporation, - Plans for Electric Rate Restructuring, Statement of Policy Regarding Vertical Market Power [encouraging divestiture], 1988 N.Y. PUC LEXIS 432; 187 P.U.R. 4th 223 (July 17, 1998). See also New York Orders approving divestiture plans. Case 96-E-0909, Central Hudson Gas & Electric Corporation - Plans for Electric Rates and Restructuring - Order Authorizing the Process for the Auctioning of Generation Plan and Modifying Prior Orders, 2000 N.Y. PUC LEXIS 93 (issued February 23, 2000); Case 96-E-0897, Consolidated Edison Company of New York. - Plans for Electric Rates and Restructuring, Order Authorizing the Process for the Auctioning of Generation Plant, 1998 N.Y. PUC LEXIS 414, 188 P.U.R. 4th 149; Case 96-E-0891, New York State Electric & Gas Corporation - Plans for Electric Rates and Restructuring, Order Authorizing the Process for the Auctioning of Generation Plant (1998 N.Y. PUC LEXIS 192 (issued April 24, 1998); Cases 94-E-0098 and 94-E-0099, Niagara Mohawk Power Corporation - PowerChoice Rate and Restructuring Plan, Order Authorizing Process for the Auctioning of Generating Facilities, 1998 N.Y. PUC LEXIS 259 (issued May 6, 1998); Case 96-E-0900, Orange and Rockland

With states serving as regulatory laboratories, retail competition is gradually taking root. See Federal Energy Regulatory Comm'n v. Mississippi, 456 U.S. 742, 788 (1982) ["Courts and commentators frequently have recognized that the 50 States serve as laboratories for the development of new social, economic and political ideas" (O'Connor, J. dissenting). See also, Connecticut Light & Power Co. v. Federal Power Comm'n, 324 U.S. 515, 529 (1945) [Congress thought it "wise to keep the hand of state regulatory bodies in this business, for the 'insulated chambers of the states' are still laboratories where many lessons in regulation may be learned by trial and error on a small scale without involving a whole national industry in every experiment"].[18] If restructuring programs are to create a fair playing field for utility competitors while protecting energy consumers from potential rate shock, regulators must assess customer needs, the capabilities of transmission and distribution infrastructures, the "margins" available in unbundled retail rates and potential competitive interests in providing unbundled services. State regulators are closest to these questions and they are prepared to implement strategies to

---

Utilities, Inc. - Plans for Electric Rates and Restructuring, Order Authorizing the Process for the Auctioning of Generation Plant and Rejecting Joint Agreement, 1998 N.Y. PUC LEXIS 259 (issued April 16, 1998); 1998 N.Y. PUC LEXIS 374.

[18] See, e.g., Application by Bell Atlantic New York for Authorization Under Section 271 of the Communications Act to Provide In-Region, InterLATA Service in the State of New York (CC Docket No. 99-295), Memorandum Opinion and Order, FCC 99-404, ¶ 6, n. 5 (December 22, 1999) [FCC decision praising state innovations that opened the door to competition].

open markets in a meaningful, effective manner.[19] Their efforts to do so, however, have been impeded by "one-size-fits-all" regulation.

---

[19] Case 98-M-0667, Electronic Data Interchange,Opinion No. 00-05, Opinion and Order on Implementation of Electronic Data Interexchange, New York Public Service Commission, 2000 N.Y. PUC LEXIS 411, 200 P.U.R. 4th 329 (April 12, 2000); Case 99-M-0631, Customer Billing Arrangements Alternative Billing Arrangements, New York Public Service Commission, Order Providing for Customer Choice of Billing Entity, 2000 N.Y. PUC LEXIS 283, 200 P.U.R. 4th 149 (issued March 22, 2000); Case 98-M-1343, Retail Access Business Rules, Opinion No. 99-3, Opinion and Order Concerning Uniform Business Practices, New York Public Service Commission, 1999 N.Y. PUC LEXIS 28, 190 P.U.R. 4th 369 (issued February 16, 1999), rehearing granted in part, 1999 N.Y. PUC LEXIS 95, (issued April 15, 1999); Case 94-E-0952, Competitive Opportunities Regarding Electric Service, New York Public Service Commission, Order Providing for Competitive Metering, 1999 N.Y. PUC LEXIS 280, 194 P.U.R. 4th 129 (issued June 16, 1999); Case 94-E-0952, Competitive Opportunities Regarding Electric Service, Opinion No. 97-13, Opinion and Order Establishing Regulatory Policies for Competitive Metering, New York Public Service Commission, 1997 N.Y. PUC LEXIS 450, 181 P.U.R. 4th 324 (issued August 1, 1997); Cases 94-E-0952 et al., Competitive Opportunities Regarding Electric Service, Opinion No. 96-12, Opinion and Order Regarding Competitive Opportunities for Electric Service, New York Public Service Commission, 1996 N.Y. PUC LEXIS 330, 168 P.U.R. 4th 515 (issued May 20, 1996).

POINT II

ENRON'S CLAIM THAT ALL TRANSMISSIONS ON THE INTERCONNECTED GRID ARE IN INTERSTATE COMMERCE IS IRRELEVANT AND, IN ANY EVENT, INCORRECT

The second principal argument of Enron's brief on the merits is that all retail transmissions on the interconnected grid are in interstate commerce. Enron's contention is irrelevant because, as indicated above, Congress assigned the states jurisdiction of all retail transactions, including retail transmissions in interstate commerce.[20] It is also, however, incorrect.[21]

---

[20] Whether a transmission is interstate is, as discussed below, governed by § 201(c), which provides that energy is transmitted interstate if it is carried from one state and consumed in another state. The definition is relevant not for determining which services FERC may regulate (FERC regulates wholesale transmissions; the states regulate retail transmissions), but for deciding which companies fall within FERC's general jurisdiction (e.g., § 203 [review and security purchases], § 204 [review and security sales]). Owners of facilities that transmit energy in interstate commerce, irrespective of whether the transmissions are retail or wholesale, are "public utilities" under § 201(e), which governs the applicability of such sections as 203 and 204 and, are therefore subject to FERC's jurisdiction. Jersey Central Power & Light v. FPC, 319 U.S. 61, 73-74 (1943) ["although a company may be a public utility under subsection (e), all of its transactions do not thereby fall under the regulatory power of the Commission. . . . [201(a)'s] limitation is directed at generation, transmission and sale"].

[21] The State Petitioners' initial brief on the merits addressed this issue (Point II.B.C., pp. 36-46); this brief will respond to the Enron

A. The Interrelationship Of Transactions On The Grid Does Not Render Retail Transmissions Interstate

In contending that all retail transmissions are in interstate commerce, Enron assumes that all transactions affect the entire grid (Enron at 6, 7). Its assumption is arguably accurate, from a theoretical standpoint, but misleading to the extent Enron uses it to suggest that all, or most, transmissions cross state lines.

If a person on a boat in the Atlantic Ocean tosses a pebble into the water, the pebble will sink and a ripple of water will appear, but there will be no other consequences. In theory, however, consistent with Enron's argument on electricity flows, the pebble's entry into the water will cause water molecules, and energy, to ripple across the entire ocean. The theory is technically correct, but inconsequential to the person in the boat because, among other things, the water molecules surrounding the boat will not travel any measurable distance.

When a customer in New York City turns on a 60 watt lightbulb, the energy required to light the bulb is supplied by increases in output of nearby New York City generators. Electric Power Research Institute (EPRI), A Primer on Electric Power Flow for Economists and Utility Planners (1995), at 2-8, 3-2; J.A. 822-823; 829-830. R. Sarikas, Introduction to Electrical Theory and Power Transmission (1995), at 70. The reaction of distant electrons in the grid is immeasurable because electrical impedance (resistance), which directs the closest power on the grid to a load, also dictates that a load change at one point on the grid has no

---

arguments that have not been answered.

appreciable impact on other areas of the grid. EPRI, supra, at 2-8, 3-2; J.A. 822-823; 829-830; Sarikas, supra, at 70.

Thus, contrary to Enron's claims (Enron at 6), all generation on the interconnected grid does not serve all customers on the grid. See B.M. Weedy, B.J. Cory, Electric Power Systems (1998) at 175 ["When large interconnected systems are linked electrically to others by means of tie-lines the power transfers between them are usually decided by mutual agreement and the power is controlled by regulators (devices that control the flow of power").]

B. Interconnections Since 1935 Are Not Relevant To The States' Jurisdiction Over Retail Transmissions

Enron alleges that although 47 states are interconnected today, only a "fraction of the nation's electric systems were interconnected" in 1935 (Enron at 7). "While in 1928, 10.7 percent of the power generated in the United States was transmitted across State lines, in 1933 more than 17.8 percent of all the energy generated in the United States flowed in interstate commerce — an amount greater than the entire amount generated in the country in 1913." 1935 Hearings on S. 1725 at 797. "Ryan-DeVane Memorandum." See also S.R. No. 74-621, at 17 (1935). Congress, therefore, understood the trend toward increased interconnections when it preserved the states pre-existing regulation of retail transmission. Inasmuch as increased interconnections since 1935 do not alter the FPA's language, they are not relevant to whether FERC may (or must) set retail transmission rates. See Arkansas Electric Coop. Corp. v. Arkansas Public Service Comm'n, 461 U.S. 375, 384, n. 8 (1983) ["Congress sought to freeze its perception of Attleboro into law . . ."].

C. The 1935 Report Further Supports State Jurisdiction Over Retail Transmission Service

Enron (Enron at 30) alleges that a report to the 1935 Congress states that interconnection facilities were subject to FERC jurisdiction. Again, facilities may be subject to FERC's jurisdiction, but the retail service they provide is subject to state regulation. The 1935 Hearings noted that Public Utilities Comm'n of Rhode Island v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927) distinguished a wholesale sale of energy across state borders, which could not be regulated by a state, from a transaction "by which gas or electric energy was transmitted across State boundaries but directly to consumers. In such a case it was held that the State in which consumption took place might regulate the rates." 1935 Hearings on H.R. 5423 at 96 (discussing Pennsylvania Gas Co. v. Public Service Comm'n, 252 U.S. 23 (1920)). Further, to the extent the cited report states that "the theory of State regulation may become obsolete" as a result of interconnections, it refers to a theory that the states may regulate the electric industry alone, without federal assistance. 1935 Hearings on H.R. 5423 at 77. ["[O]nce the industry begins to transcend State boundaries either by physical interconnections or by subtle business and financial affiliations the theory of State regulation may become obsolete. . . . attempts by the individual States to extend their laws to cover the holding-company system are met with more serious jurisdictional objections."]

D. The Case Law Cited By Enron Does Not Support Its Position

Enron argues that Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453, 463 (1972) stands for the proposition that all transmissions on interstate grids are

FERC-jurisdictional.[22] Florida Power & Light neither accepted nor rejected the theory that all generators on an interconnected grid provide a pool of interstate energy that services all load requirements throughout the grid (Enron 28, 30). The Court found it unnecessary to approve or disapprove an "analysis based upon unity of electromagnetic response" (404 U.S. at 461-62).

Enron also relies (Enron at 31) on a statement from Northern States Power Co. v. Federal Energy Regulatory Comm'n, 30 F.3d 177, 179 (D.C. Cir. 1994), that "[t]here is no way to determine what path electricity actually takes between two points or indeed whether the electricity at the point of delivery was ever at the point of origin." Congress addressed the possibility that electricity generated in one state and used in that state might take a path outside state boundaries. It provided in FPA § 201(c) that electricity would only be in interstate commerce if it was produced in one state and consumed in another state.

---

[22] Enron relies upon Justice Douglas' dissent from the supposed result of Florida Power & Light that "the commingled method will now mean that every privately owned interconnected facility in the United States (except for those isolated in Texas) is within the [FERC's] jurisdiction." 404 U.S. at 471 (Douglas, J. dissenting). Justice Douglas, however, also noted "[a]ll that is involved here is an effort to make [Florida Power & Light] follow [FERC's] Uniform System of Accounts." 404 U.S. at 472-73 (Douglas, J. dissenting).

CONCLUSION

For the reasons indicated above, Enron's challenge to FERC's Orders 888 and 888-A should be rejected.

Respectfully submitted,

Lawrence G. Malone*
General Counsel
Jonathan D. Feinberg
Carl F. Patka
Diane T. Dean
Assistant Counsel
NYS Public Service Commission
Three Empire State Plaza
Albany, New York 12223-1350
(518) 474-2510

Counsel of Record

Dated: May 2001
Albany, NY

James Bradford Ramsay
General Counsel
Sharla Barklind
Assistant General Counsel
National Association of Regulatory
Utility Commissioners
1101 Vermont Avenue, Suite 200
Washington, D.C. 20005
(202) 898-2208

Catherine D. Bedell
General Counsel
Richard Bellak
Associate General Counsel
Florida Public Service
Commission
2540 Shumard Oak Boulevard
Capital Circle Office Center
Tallahassee, FL 32399-0850
(850) 413-6092

Alan G. Lance
Attorney General
Donald L. Howell, II
Deputy Attorney General
Idaho Public Utilities
Commission
472 W. Washington Street
P.O. Box 83720
Boise, ID 83720-0074
(208) 334-0312

John J. Farmer, Jr.
Attorney General
State of New Jersey
Helene S. Wallenstein
Sr. Deputy Attorney General
Attorney for New Jersey Board
of Public Utilities
124 Halsey Street, 5th Floor
P.O. Box 45029
Newark, New Jersey 07101
(973) 648-4846

Jo Anne Sanford
North Carolina Utilities Comm'n
Robert P. Gruber
Public Staff - North Carolina
Utilities Comm'n
Gisele L. Rankin
Staff Attorney
4326 Mail Service Center
Raleigh, NC 27699-4326
(919) 733-2435

William H. Chambliss
General Counsel
C. Meade Browder, Jr.
Associate General Counsel
Virginia State Corporation Comm'n
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218
(804) 371-9671

Christine O. Gregoire
Attorney General
William Berggren Collins
Sr. Assistant Attorney General
Robert D. Cedarbaum
Senior Counsel
(for the Washington Utilities and
Transportation Commission)
P.O. Box 40128
Olympia, WA 98504-0128
(360) 664-1188

Harvey L. Reiter
(for the Vermont Department of Public Service)
Morrison & Hecker.
1150 18th Street, N.W.
Suite 800
Washington, D.C. 20036
(202) 785-9100

Harry Ivey
(for the Wyoming Public Service Commission)
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002
(307) 777-7824

Supreme Court, U.S.
FILED
MAY 31 2001
MAY 31 2001
CLERK

Nos. 00-568 and 00-809

In the Supreme Court of the United States

STATE OF NEW YORK, ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ENRON POWER MARKETING, INC., PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ON WRITS OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

KEVIN P. MADDEN
General Counsel
CYNTHIA A. MARLETTE
Deputy General Counsel
SUSAN J. COURT
Associate Solicitor
TIMM L. ABENDROTH
DAVID H. COFFMAN
Attorneys
Federal Energy Regulatory Commission
Washington, D.C. 20426

BARBARA D. UNDERWOOD
Acting Solicitor General
Counsel of Record
EDWIN S. KNEEDLER
Deputy Solicitor General
AUSTIN C. SCHLICK
Assistant to the Solicitor General
Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

QUESTIONS PRESENTED

In its Order No. 888, the Federal Energy Regulatory Commission found that public utilities subject to its jurisdiction under the Federal Power Act (FPA or Act), 16 U.S.C. 791a *et seq.*, had discriminated unlawfully in providing access to their facilities for transmitting electric power, and had the ability and incentive to continue to do so. As a remedy, Order No. 888 requires those utilities to provide nondiscriminatory access to their transmission systems, thereby facilitating competition in the market for electric energy.

1. In No. 00-568, the question presented is whether the court of appeals correctly determined that Section 201 of the FPA, 16 U.S.C. 824, authorizes the Commission to exercise jurisdiction over the service of transmitting in interstate commerce electric energy that is sold at retail, where the transmission service is "unbundled" from the State-regulated retail sale of energy and the retail customer has the ability to choose a preferred power supplier.

2. In No. 00-809, the question presented is whether the court of appeals properly deferred to the Commission's determination that it lacks jurisdiction over retail transmission service that is sold together with electric energy in a single "bundled" transaction between a public utility and its retail customer, where the retail customer cannot choose a preferred power supplier.

PARTIES TO THE PROCEEDING

The petitioners and intervenors in the court of appeals are set forth in Volume II of the Petition Appendix in No. 00-568 at R1-R7 and in Volume II of the Petition Appendix in No. 00-809 at 683a-688a.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	2
Statutory provisions involved	2
Statement	2
Summary of argument	19
Argument	22
I. The Commission correctly interpreted the Federal Power Act as establishing federal jurisdiction over unbundled transmission of electric energy in interstate commerce	22
A. Transmission by a utility that utilizes an interstate grid is "in interstate commerce"	23
B. Congress did not exclude unbundled retail transmission from the commission's jurisdiction over interstate transmission	28
C. The Commission's jurisdictional holding is consistent with Congress's purposes in enacting Section 201	34
D. Policy considerations also do not support New York's interpretation	42
II. The Commission reasonably concluded that Congress has not authorized federal regulation of the transmission component of bundled retail sales of electric energy	44
Conclusion	50

TABLE OF AUTHORITIES

Cases:

Arcadia v. *Ohio Power Co.*, 498 U.S. 73 (1990)	6
Arkansas Elec. Coop. Corp. v. *Arkansas Pub. Serv. Comm'n*, 461 U.S. 375 (1983)	24, 38, 41

Cases—Continued: Page

Arkansas La. Gas Co. v. *Hall*, 453 U.S. 571 (1981) 29
Attleboro Steam & Elec. Co. v. *Public Utils. Comm'n* 129 A. 495 (R.I. 1925), aff'd, 273 U.S. 83 (1927) 37
California v. *FERC*, 495 U.S. 490 (1990) 41
California v. *Lo-Vaca Gathering Co.*, 379 U.S. 366 (1965) 26
CFTC v. *Schor*, 478 U.S. 833 (1986) 49
Chemehuevi Tribe of Indians v. *FPC*, 420 U.S. 395 (1975) 42
Chevron U.S.A. Inc. v. *Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984) 18, 45, 48, 49
Connecticut Light & Power Co. v. *FPC*, 324 U.S. 515 (1945) ..... *passim*
Dole v. *United Steelworkers*, 494 U.S. 26 (1990) 49
FERC v. *Mississippi*, 456 U.S. 742 (1982) 10
FPC v. *Conway Corp.*, 426 U.S. 271 (1976) 43
FPC v. *East Ohio Gas Co.*, 338 U.S. 464 (1950) 29, 33
FPC v. *Florida Power & Light Co.*, 404 U.S. 453 (1972) 17, 19, 24, 25, 26, 27, 28
FPC v. *Louisiana Power & Light Co.*, 406 U.S. 621 (1972) 20, 29, 38, 41, 47
FPC v. *Southern Cal. Edison Co.*, 376 U.S. 205 (1964) 8, 30, 34, 35
FPC v. *Sunray DX Oil Co.*, 391 U.S. 9 (1968) 27
General Motors Corp. v. *Tracy*, 519 U.S. 278 (1997) 33
Glover v. *United States*, 121 S. Ct. 696 (2001) 27
Gulf States Utils. Co. v. *FPC*, 411 U.S. 747 (1973) 5, 6
Indiana Mich. Power Co., 64 F.E.R.C. ¶ 61,184 (1993) 5
Jersey Cent. Power & Light Co. v. *FPC*, 319 U.S. 61 (1943) 17, 24
Louisiana Pub. Serv. Comm'n v. *FCC*, 476 U.S. 355 (1986) 41-42
Maislin Indus., Inc. v. *Primary Steel, Inc.*, 497 U.S. 116 (1990) 41
Mississippi Power & Light Co. v. *Mississippi*, 487 U.S. 354 (1988) 49

Cases—Continued: Page

NLRB v. *City Disposal Sys., Inc.*, 834 F.2d 191 (D.C. Cir. 1987) 49
New England Power Co. v. *New Hampshire*, 455 U.S. 331 (1982) 7, 8-9, 24, 41, 46
Northern States Power Co. v. *FERC*, 176 F.3d 1090 (8th Cir. 1999), cert. denied, 528 U.S. 1182 (2000) 48
Northern States Power Co. (Minn.), 89 F.E.R.C. ¶ 61,178 (1999) 49
Panhandle E. Pipeline Co. v. *Public Serv. Comm'n*, 332 U.S. 507 (1947) 29
Pennsylvania Gas Co. v. *Public Serv. Comm'n*, 252 U.S. 23 (1920) 33-34
Public Utils., Comm'n v. *Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927) 5, 7, 8
San Diego Gas & Elec. Co. v. *Sellers of Energy and Ancillary Servs. into Mkts. Operated by the Cal. Indep. Sys. Operator and the Cal. Power Exch.*, 93 F.E.R.C. ¶ 61,121 (2000), mandamus denied, 245 F.3d 1110 (9th Cir. 2001) 44
Solid Waste Agency v. *United States Army Corps of Eng'rs*, 121 S. Ct. 675 (2001) 40
United Distribution Cos. v. *FERC*, 88 F.3d 1105 (D.C. Cir. 1996) 29
United States v. *Public Utils. Comm'n*, 345 U.S. 295 (1953) 5, 34, 41, 46
West v. *Gibson*, 527 U.S. 212 (1999) 40
Western Power Trading Forum v. *FERC*, 245 F.3d 798 (D.C. Cir. 2001) 44

Constitution, statutes, regulation and rule:

U.S. Const. Art. I, § 8, Cl. 2 (Commerce Clause) 7
Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776 10
Federal Power Act, 16 U.S.C. 791a *et seq.* 6

Statutes, regulation and rule—Continued: Page

Pt. II, 16 U.S.C. 824-824m 2
§§ 201-214, 16 U.S.C. 824-824m 6
§ 201, 16 U.S.C. 824 ..... *passim*
§ 201(a), 16 U.S.C. 824(a) 6, 20, 34, 46
§ 201(b), 16 U.S.C. 824(b) ..... *passim*
§ 201(b)(1), 16 U.S.C. 824(b)(1) ..... *passim*
§ 201(c), 16 U.S.C. 824(c) 7, 23, 25
§ 201(d), 16 U.S.C. 824(d) 8
§ 201(e), 16 U.S.C. 824(e) 6
§ 201(f), 16 U.S.C. 824(f) 6
§ 205, 16 U.S.C. 824d 12, 25
§ 205(a), 16 U.S.C. 824d(a) 7
§ 205(b), 16 U.S.C. 824d(b) 7
§ 205(c), 16 U.S.C. 824d(c) 7
§ 206, 16 U.S.C. 824e 12, 25, 49, 50
§ 206(a), 16 U.S.C. 824e(a) 7, 50
§ 206(d), 16 U.S.C. 824e(d) 35, 36, 37, 38
§ 211, 16 U.S.C. 824j 10
§ 212, 16 U.S.C. 824k 10
§ 212(h), 16 U.S.C. 824k(h) 15, 36
§ 212(h)(1), 16 U.S.C. 824k(h)(1) 16
§ 313, 16 U.S.C. 825*l*(b) 27
Natural Gas Act, 15 U.S.C. 717 *et seq.* 28
§ 1(b), 15 U.S.C. 717(b) 20, 29, 33
§ 1(c), 15 U.S.C. 717(c) 33
Public Utility Act of 1935, ch. 687, 49 Stat. 803 5
Public Utility Holding Company Act, ch. 687, Tit. I, §§ 1-33, 15 U.S.C. 79a-79z-5 6
Public Utility Regulatory Policies Act of 1978, Pub. L. No. 95-617, 92 Stat. 3117 10
§ 210, 16 U.S.C. 824a-3 10
18 C.F.R. 35.28(c) 43
Sup. Ct. R. 14(a) 28

Miscellaneous: Page

Energy Information Administration, U.S. Dep't of Energy:
Status of State Electric Industry Restructing Activity as of May 2001 (May 2001) (available at <http://www.eia.doe.gov/cneaf/electricity/chg-str/regmap.html>) 44
The Changing Structure of the Electric Power Industry 2000: An Update (Oct. 2000) (available at <http://www.eia.doe.gov/cneaf/electricity/chg-stru-/update/update2000.html>) 3-4, 5, 9, 11
61 Fed. Reg. (1996):
p. 21,540 13
pp. 21,628-21,664 13
H.R. Rep. No. 1318, 74th Cong., 1st Sess. (1935) 9, 36, 46
Public Utilities Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce, 74th Cong., 1st Sess., Pt. 2 (1935) 27, 39
Regional Transmission Orgs., Order No. 2000, 65 Fed. Reg. 809, on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (2000), appeal pending *sub nom. Public Utils. Dist. No. 1* v. *FERC*, No. 00-1174 (D.C. Cir.) 48
H. Rustebakke, *Electric Utility Systems and Practices* (4th ed. 1983) 3, 31
S. Rep. No. 621, 74th Cong., 1st Sess. (1935):
Pt. 1 ..... 8, 9, 30, 37, 38, 46
Pt. 2 26
R. Sarikas, *Introduction to Electrical Theory and Power Transmission* (1995) 4

In the Supreme Court of the United States

No. 00-568

STATE OF NEW YORK, ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

No. 00-809

ENRON POWER MARKETING, INC., PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ON WRITS OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE
FEDERAL ENERGY REGULATORY COMMISSION

OPINIONS BELOW

The opinion of the court of appeals (1 Pet. App. 3a-121a)[1] is reported at 225 F.3d 667. The relevant orders of the Federal Energy Regulatory Commission are reported as follows: Order No. 888, 61 Fed. Reg. 21,540 (1996) (excerpted at 1 J.A. 42-430), and Order No. 888-A, 62 Fed. Reg. 12,274 (1997) (excerpted at 2 J.A. 517-791).

[1] Unless otherwise indicated, all references to "Pet. App." are to the petition appendix in No. 00-809. We refer to the state petitioners in No. 00-568, collectively, as "New York."

JURISDICTION

The judgment of the court of appeals (1 Pet. App. 1a-2a) was entered on June 30, 2000. Petitions for rehearing were denied on August 22, 2000 (1 Pet. App. 123a-124a). The petition for certiorari in No. 00-568 was filed on October 12, 2000. The petition in No. 00-809 was filed on November 20, 2000. The petitions were granted on February 26, 2001. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTORY PROVISIONS INVOLVED

Relevant provisions of Part II of the Federal Power Act, 16 U.S.C. 824-824m, are set out at 2 Pet. App. 652a-681a.

STATEMENT

This case involves one of the critical jurisdictional underpinnings of the Federal Energy Regulatory Commission's program for promoting competition in the electric power industry. Commission Order No. 888 requires public utilities to "unbundle" their generation and wholesale sales of electric power from their wholesale transmission of electric power, and to provide other power suppliers nondiscriminatory access to their transmission systems. Unbundling and "open access" to transmission systems enable energy producers to deliver electric power across the Nation's interstate power grids, and prevent utilities from using their control over essential transmission systems to undermine the increasingly competitive market for electric energy.

When crafting Order No. 888, the Commission exercised its jurisdiction in accordance with Part II of the Federal Power Act (FPA or Act), 16 U.S.C. 824-824m. Broadly speaking, Section 201 of the FPA gives the Commission jurisdiction over the transmission and wholesale sale of electric energy in interstate commerce, while leaving regulation of local distribution and retail sales of electric energy to the States. 16 U.S.C. 824. The Commission interpreted Section 201 as preserving the States' historical jurisdiction over

traditional monopoly arrangements—under which retail customers buy electric energy, transmission service, and local distribution service from a single, regulated supplier for a single charge. Accordingly, under Order No. 888, States may continue to regulate the entirety of those bundled retail sales, just as before. But if a public utility voluntarily permits retail customers to purchase power from competing suppliers, or if a State chooses to require such competition, then the Commission's new open-access rule would extend to the utility's separately offered service of transmitting electric energy in interstate commerce in connection with the unbundled retail sale of energy. Even in that case, however, the State would continue to have exclusive jurisdiction over the retail sale of energy and over local distribution of the energy.

The court of appeals found that the Commission's approach is consistent with the jurisdictional rules established by Congress in the FPA. 1 Pet. App. 27a-39a. The court rejected the argument of some States that the Commission may not regulate *unbundled* transmission of electric power that is associated with retail sales. At the same time, the court rejected the argument of some industry members that the Commission was required to apply the provisions of its standard open-access transmission tariff to *bundled* retail sales that historically have been regulated by the States.

1. Electric power systems have three basic functions: generating electric energy, transmitting the energy in bulk, and distributing it to consumers. Electric energy is generated at a generating station, and its voltage is increased ("stepped up") for transmission over high-voltage lines. After the energy travels to the vicinity of the end user over transmission lines, its voltage is reduced ("stepped down") for delivery over a local distribution system.[2]

---

[2] See H. Rustebakke, *Electric Utility Systems and Practices* 1, 13-26 (4th ed. 1983) (describing typical power systems); Energy Information

Power systems in the continental United States are organized into three major networks, or "grids": the Eastern Interconnect, the Western Interconnect, and the Texas Interconnect (which covers most of Texas). Each grid is formed by high-voltage connections that are used to transfer electric energy from one utility on the grid to another. The Eastern Interconnect and the Western Interconnect are themselves connected. See *Electric Power Industry 2000* 13-14 & Fig. 7. Wholesale exchanges of power over the grids enable utilities to obtain electric energy from sources other than their own generating plants. The grids therefore provide utilities with access to lower-cost sources of power and improve the reliability of the utilities' services. *Id.* at 23. Today, "[v]irtually all" utilities in the continental United States are connected to a major grid. *Id.* at 14. Physically isolated power systems "have become a thing of the past." 2 Pet. App. 584a-585a.

Within each grid, electric energy follows the path of least resistance. The energy divides among multiple paths—which may or may not be owned by the utility that generates or sells the power—in order to find the path of least resistence between the generating station and the demand for power ("load"). 2 Pet. App. 612a & n.144. That flow of energy over parallel paths, known as "loop flow," is inevitable unless there is a direct ("radial") connection between the generation facility, at one end, and the load, at the other. See *ibid.*; R. Sarikas, *Introduction to Electrical Theory and Power Transmission* 56-57 (1995) (discussing radial transmission). Accordingly, "if any part of a supply of electric energy comes from outside of a state it is, or may be, present

Administration, U.S. Dep't of Energy, *The Changing Structure of the Electric Power Industry 2000: An Update* (*Electric Power Industry 2000*) 9-16 (Oct. 2000) (available at <http://www.eia.doe.gov/cneaf/electricity/chg_stru_update/update2000.html>); see also *Connecticut Light & Power Co.* v. *FPC*, 324 U.S. 515, 519-521 (1945) (describing utility's facilities).

in every connected distribution facility." *Connecticut Light & Power Co.* v. *FPC*, 324 U.S. 515, 529 (1945).[3]

2. The interconnected nature of transmission grids, and their use in interstate commerce, have increased dramatically since 1935, when Congress enacted the relevant provisions of the FPA. At that time, the electric power industry was composed of largely self-sufficient utilities with their own generation, transmission, and distribution facilities. Vertically integrated electric utilities were deemed natural monopolies, and they sold their generation, transmission, and distribution services as a single bundled service to wholesale and retail customers, under the oversight of state regulators. 1 J.A. 190; 2 Pet. App. 578a; *Electric Power Industry 2000* 5. Because electric energy could not yet be transmitted efficiently over long distances, local utilities were not linked into large, centralized systems. See *United States* v. *Public Utils. Comm'n (California PUC)*, 345 U.S. 295, 302 (1953). Nevertheless, local monopolies did interconnect with neighboring utilities, and issues arose around exchanges of electric energy in interstate commerce, which were beyond the States' power to regulate. See, *e.g.*, *Public Util. Comm'n* v. *Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927). States likewise were unable to regulate the financial practices of the interstate holding companies that controlled many local utilities. The practices of those holding companies came under heavy criticism during the 1920s and early 1930s. See *Gulf States Utils. Co.* v. *FPC*, 411 U.S. 747, 758 (1973); *Electric Power Industry 2000* 5.

Congress enacted the Public Utility Act of 1935, ch. 687, 49 Stat. 803, to address those concerns. The Public Utility

[3] Utilities typically contract to transmit power for each other "as if power flowed along one series of lines belonging to specific owners." 2 Pet. App. 612a. But "in reality power flows are rarely confined to a designated contract path." *Id.* at 612a n.144 (quoting *Indiana Mich. Power Co.*, 64 F.E.R.C. ¶ 61,184 (1993)).

Act "had two primary and related purposes." *Gulf States Utils.*, 411 U.S. at 758. First, Congress sought "to curb abusive practices of public utility companies by bringing them under effective control," which was the subject of Title I of the 1935 Act, known as the Public Utility Holding Company Act (§§ 1-33, 15 U.S.C. 79a through 79z-5.). See *Arcadia* v. *Ohio Power Co.*, 498 U.S. 73, 75 (1990). Second, Congress wanted "to provide effective federal regulation of the expanding business of transmitting and selling electric power in interstate commerce," which was the subject of the provisions of the 1935 Act that became Part II of the FPA. *Gulf States Utils.*, 411 U.S. at 758. Part II of the FPA (§§ 201-214, 16 U.S.C. 824-824m) conferred on the Commission's predecessor (the Federal Power Commission (FPC)) jurisdiction over specified activities of "public utilit[ies]," which as a practical matter meant investor-owned utilities as distinguished from, for example, municipal utilities. See 16 U.S.C. 824(e) and (f).[4]

In Section 201(a) of the FPA, 16 U.S.C. 824(a), Congress "declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest." Congress further declared that federal regulation of power generation, transmission of electric energy in interstate commerce, and the sale of electric energy at wholesale in interstate commerce, as provided in the Act, "is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States." 16 U.S.C. 824(a).

Section 201(b), the principal jurisdictional provision of Part II of the FPA, provides in pertinent part that the federal regulatory scheme "shall apply to the transmission of electric energy in interstate commerce and to the sale of

[4] The Public Utility Act of 1935 also amended the hydroelectric power provisions now found in Part I of the FPA, 16 U.S.C. 791a *et seq.*

electric energy at wholesale in interstate commerce, but [with limited exceptions] shall not apply to any other sale of electric energy." 16 U.S.C. 824(b)(1). Section 201(b) further grants the Commission "jurisdiction over all facilities for such transmission or sale of electric energy," but generally denies the Commission jurisdiction "over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce." 16 U.S.C. 824(b)(1).

Section 201(c) provides that electric energy is transmitted in interstate commerce, for purposes of Part II, if it is "transmitted from a State and consumed at any point outside thereof" (but within the United States). 16 U.S.C. 824(c).

The substantive provisions of Part II prohibit, among other things, unjust or unreasonable rates, and undue discrimination "with respect to any transmission or sale subject to the jurisdiction of the Commission." 16 U.S.C. 824d(a) and (b) (FPA § 205(a) and (b)). Section 205(c) requires public utilities to file tariff schedules with the Commission, under such rules and in such form as the Commission may prescribe, showing their rates and terms for service, along with related contracts for service. 16 U.S.C. 824d(c). If the Commission finds that a public utility's rate "for any transmission or sale subject to the jurisdiction of the Commission," or any practice "affect[ing] such rate," is "unjust, unreasonable, unduly discriminatory or preferential," the Commission must prescribe a lawful rate or practice for the future. 16 U.S.C. 824e(a) (FPA § 206(a)).

Part II of the FPA was intended in part to "fill the gap" between federal and state jurisdiction created by *Public Utilities Commission* v. *Attleboro Steam & Electric Co.*, *supra*. See *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 340 (1982). In *Attleboro*, the Court had held that the Commerce Clause prohibited Rhode Island (or Massachusetts) from regulating the rates charged by a Rhode Island utility for electricity delivered to a separate

utility in Massachusetts, and that only Congress could regulate that wholesale transaction across state lines. See 273 U.S. at 84, 89-90. Part II of the Act filled the jurisdictional void created by *Attleboro* by establishing exclusive federal jurisdiction over such transactions. *New England Power*, 455 U.S. at 340.

When drafting the FPA, Congress understood that *Attleboro* and earlier cases established that the States could not regulate "any wholesale [power] transaction in interstate commerce." *FPC* v. *Southern Cal. Edison Co. (Colton)*, 376 U.S. 205, 213 n.8 (1964) (citing legislative history). Congress therefore extended federal regulation "to the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. 824(b)(1) (FPA § 201(b)(1)). Distinguishing wholesale sales from retail sales drew "a bright line easily ascertained" between federal and state jurisdiction. *Colton*, 376 U.S. at 215; see 16 U.S.C. 824(d) ("sale of electric energy at wholesale" means "a sale of electric energy to any person for resale").

The *Attleboro* Court also had broadly held that "[t]he transmission of electric current from one State to another * * * is interstate commerce." 273 U.S. at 86. Accordingly, and consistent with its goal of simplifying the process of deciding whether a particular transaction is subject to federal or state regulation, see *Colton*, 376 U.S. at 214-216, Congress included in Section 201(b)(1) an additional grant of federal jurisdiction over "interstate transmission," without any language limiting that jurisdiction to wholesale transactions. 16 U.S.C. 824(b)(1); see S. Rep. No. 621, 74th Cong., 1st Sess., Pt. 1, at 17, 19 (1935) (noting that "[o]ther features of th[e] interstate utility business," besides interstate wholesale transactions, are "immune from State control," and that federal jurisdiction under Section 201(b) "includes interstate transmission where there is no sale").

At the same time, Congress intended to "tak[e] no authority from State commissions." *New England Power*, 455 U.S.

at 341 (quoting H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935)) (emphasis omitted). It instead wanted to establish federal regulation "over those matters which cannot effectively be controlled by the States." S. Rep. No. 621, *supra*, Pt. 1, at 18. To that end, Congress provided that (as a general matter) the Commission's jurisdiction would not extend "to any other sale of electric energy" not made the subject of federal regulation in Section 201(b). 16 U.S.C. 824(b)(1). Furthermore, while the FPC would "have jurisdiction over all facilities for such transmission or sale of electric energy" within its jurisdiction,[5] as noted above the FPC was denied general jurisdiction "over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce." 16 U.S.C. 824(b)(1).[6]

3. By the 1970s, technological changes were beginning to erode the natural monopoly character of the vertically integrated utilities. Relatively small and inexpensive generating plants, generally fueled by natural gas, came over time to provide a cost-competitive alternative to the utilities' large, capital-intensive plants. See 1 J.A. 61-67; *Electric Power Industry 2000* 44-45. Continued improvements in transmission technologies made it possible to transmit electric power at higher voltages over longer distances, so that utilities with lower-cost plants or excess capacity could sell

---

[5] The Senate report explained that "[j]urisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines," because "no steps can be taken to secure the planned coordination of this industry on a regional scale unless all of the facilities, other than those used solely for retail distribution, are made subject to the jurisdiction of the Commission." S. Rep. No. 621, *supra*, Pt. 1, at 48. In the final bill, Congress assigned jurisdiction over generation facilities to the States rather than to the Commission. 16 U.S.C. 824(b)(1).

[6] Congress likewise did not assert federal jurisdiction "over facilities for the transmission of electric energy consumed wholly by the transmitter." 16 U.S.C. 824(b)(1).

their power to customers as many as 1000 miles away. 1 J.A. 67-68.

Federal legislation accelerated competition in the generation of electric power. Congress enacted the Public Utility Regulatory Policies Act of 1978 (PURPA), Pub. L. No. 95-617, 92 Stat. 3117, to promote the development of alternative generating facilities that conserve traditional fossil fuels. 1 J.A. 68-70; see *FERC* v. *Mississippi*, 456 U.S. 742, 745-751 (1982). Among other things, PURPA required utilities to purchase power from the new alternative producers. See 16 U.S.C. 824a-3. The ensuing proliferation of alternative generation facilities demonstrated that vertically integrated public utilities need not be the only source of reliable power. 1 J.A. 70.

Other non-traditional sellers of electric power entered the market as well. They included independent power producers, which do not own any transmission or distribution facilities; affiliates of traditional utilities; and power marketers (such as Enron Power Marketing, Inc., the petitioner in No. 00-809), which sell power without owning the physical facilities used in connection with the sale. See 1 J.A. 71-73.

By the 1990s, problems involving access to the traditional utilities' transmission facilities had become a critical obstacle to the continued development of cheaper and more efficient sources of electric power. 1 J.A. 73-77. As the court of appeals explained in this case, "[p]ower generators not permitted to use utilities' transmission lines on reasonable terms have no way to transmit their power to customers." 1 Pet. App. 11a. In the Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776, Congress authorized the Commission to order utilities to provide transmission service, known as "wheeling," on a case-by-case basis for wholesale transactions. See 16 U.S.C. 824j, 824k (FPA §§ 211, 212); 1 J.A. 77-78. In practice, however, case-by-case consideration of wheeling requests entailed significant delays that limited the practical value of wheeling. 1 J.A. 81-83. So too, the Commission's powers to require nondiscrimination when utilities voluntarily offered transmission services to other generators, and in connection with utility mergers, were limited because they could be exercised only in those contexts. See 1 J.A. 83-90.

4. a. By the mid-1990s, new generating facilities were producing power at as little as one-fifth of the cost of electricity generated by the traditional utilities' most expensive large plants. See 1 J.A. 97. Consumers (particularly large industrial users) who paid high electric rates were demanding access to lower-priced energy. 1 J.A. 97-98; see *Electric Power Industry 2000* 41-44.

The Commission responded by, among other things, issuing in March 1995 the notice of proposed rulemaking (2 Pet. App. 553a-644a) that led to Order No. 888.[7] The Commission proposed to require public utilities to offer nondiscriminatory transmission services for wholesale power sales under standard tariff terms. See *id.* at 559a-560a. In proposing "open access," the Commission reasoned that the traditional utilities' exercise of "market power through control of transmission is the single greatest impediment to competition" in bulk power markets. *Id.* at 558a. "Transmission is the vital link between sellers and buyers," the Commission explained. *Ibid.* "To achieve the benefits of robust, competitive bulk power markets, all wholesale buyers and sellers must have equal access to the transmission grid. Otherwise, efficient trades cannot take place and ratepayers will bear unnecessary costs." *Ibid.*

b. In April 1996, the Commission issued Order No. 888 (1 J.A. 42-430). Based on comments submitted in response to its notice of proposed rulemaking, the Commission found

---

[7] The Commission also initiated other proceedings "[t]o address the fact that the electric industry is becoming more competitive, and to remove barriers that might inhibit a more competitive industry." 1 J.A. 91-92 (listing Commission initiatives).

that public utilities were commonly discriminating in violation of Section 205 of the FPA, 16 U.S.C. 824d, by denying access to their transmission networks or providing only inferior access. 1 J.A. 178-191. The Commission determined that such discrimination would likely "increase as competitive pressures continue to grow in the industry, unless the Commission acts now to prevent such practices." 1 J.A. 185.

Invoking its authority under Sections 205 and 206 of the FPA to remedy the unlawful discrimination it had identified, the Commission required "functional unbundling" of wholesale interstate transmission services. 1 J.A. 106. Specifically, a public utility that owns or controls transmission facilities must: (1) obtain transmission service for its own wholesale transactions under terms and conditions set out in the same tariff of general applicability that the utility offers to unaffiliated transmission customers; (2) separately state rates for wholesale generation and transmission, as well as for "ancillary services" (such as scheduling and correction of energy imbalances) that are needed for basic transmission service; and (3) when using the generally available transmission service, obtain information about its own transmission system by means of the same electronic information network that is made available to unaffiliated transmission customers. 1 J.A. 106-107. The Commission published a pro forma tariff containing minimum terms and conditions for nondiscriminatory open-access service, and required utilities to file tariffs containing those terms. 1 J.A. 52; see 1 J.A. 683-691 (pro forma tariff). The Commission declined, however, to order "a more intrusive and potentially more costly mechanism" for addressing discrimination—requiring utilities to divest their transmission facilities. 1 J.A. 108-109.[8]

[8] The Commission additionally addressed the problem of "stranded costs," *i.e.*, a utility's inability to recoup its sunk costs when wholesale customers take advantage of open access to purchase power from other suppliers. In general, Order No. 888 allows a utility to recover such costs from a former customer if the utility is able to show a "reasonable expectation" that, absent open access, it would have continued to sell power to the customer. See 61 Fed. Reg. 21,540, 21,628-21,664 (1996).

The Commission estimated that, as a result of its open-access requirement, consumers would realize cost savings of approximately $3.8 to $5.4 billion per year. 1 J.A. 99. The Commission also noted that at least 12 States, responding to the same market opportunities for consumer savings and economic growth, had taken steps to give retail customers a choice of power suppliers. 1 J.A. 95 & n.101.

The Commission recognized that its unbundling rule implicated the allocation of jurisdiction over electric power services between the federal government and the States. In its lengthy analysis of jurisdictional issues, see 1 J.A. 384-430, the Commission concluded that when a public utility delivers electric energy in interstate commerce from a third-party supplier to a purchaser who will resell it, Section 201(b) of the FPA provides the Commission exclusive jurisdiction over the rates, terms, and conditions of that transmission service and any facilities used to provide it, even if those facilities might also be labeled "local distribution" facilities. 1 J.A. 425-426.

The Commission next concluded that it also has jurisdiction over unbundled transmission services, and the facilities used to provide those services, where the power is transmitted in interstate commerce to *retail* customers who have the ability to choose their energy supplier. The Commission found it particularly "compelling" that Section 201 gives the Commission jurisdiction over public utilities' transmission of energy in interstate commerce "without qualification" and, in particular, without any limitation to transmission in connection with wholesale transactions. 1 J.A. 348-349. The Commission considered the illustrative

example of a retail customer who purchases energy in interstate commerce from a distant supplier, using the lines of intermediate utilities as well as the lines of the customer's previous power supplier. 1 J.A. 427. In that situation, the Commission determined that it would have jurisdiction over all the transmission facilities used by the intervening utilities to deliver the power. *Ibid.*

"The more difficult issue," however, was "whether some portion of the facilities used to transmit energy from the transmitting utility in closest proximity to the end user (the former supplier of the bundled product) [would be] local distribution facilities," and thus expressly subject to state regulation under Section 201(b)(1). 1 J.A. 427. The Commission concluded that "in most, if not all circumstances, some portion will be local distribution facilities." *Ibid.*; see also 1 J.A. 348. The Commission therefore identified seven "indicators" it will consider in determining whether particular facilities a public utility uses for its unbundled transmission of power for sale at retail are transmission facilities subject to federal jurisdiction in that context, or instead are local distribution facilities subject to state jurisdiction. 1 J.A. 428-429; see 1 J.A. 354-358.[9] The Commission stated, however, that, in order to avoid regulatory conflict and to take advantage of state regulators' expertise, it would defer to recommendations by state commissions when applying its seven factors. 1 J.A. 356-357.

[9] The seven indicators are that: (1) local distribution facilities are normally in close proximity to retail customers; (2) local distribution facilities are primarily radial in character; (3) power flows into local distribution systems, but rarely out; (4) power that enters a local distribution system is not reconsigned or transported on to some other market; (5) power entering a local distribution system is consumed in a comparatively restricted geographical area; (6) meters measure flows into the local distribution system; and (7) local distribution systems have reduced voltage. 1 J.A. 322.

The Commission emphasized that it was not claiming authority over any part of traditional arrangements in which the public utility bundles the retail sale of power together with the transmission of that power. "[W]hen transmission is sold at retail as part and parcel of the delivered product called electric energy," the Commission explained, "the transaction is a sale of electric energy at retail," and therefore regulated by the States under Section 201(b). 1 J.A. 349. But when electric energy is sold separately from transmission, potentially by another supplier, "the jurisdictional lines change." 1 J.A. 349-350. "In this situation," the Commission reasoned, "the state clearly retains jurisdiction over the sale of the power. However, the unbundled transmission service involves *only* the provision of 'transmission in interstate commerce' which, under the FPA, is exclusively within the jurisdiction of the Commission." 1 J.A. 350 (emphasis added).[10]

Relatedly, the Commission emphasized that in exercising jurisdiction over the rates, terms, and conditions of the unbundled transmission of power for sale at retail, it was not asserting jurisdiction to order utilities to unbundle their retail services, or to order transmission to any retail consumer. 1 J.A. 350; see also 1 J.A. 226-227 (finding unbundling of retail transmission and generation unnecessary to eliminate discrimination and declining to order it for that reason and due to jurisdictional concerns). Indeed, the Commission noted, Section 212(h) of the FPA, 16 U.S.C. 824k(h), "clearly prohibits" the Commission from ordering

[10] In practice, a power supplier that competes with the local public utility to serve an ordinary retail consumer typically serves that consumer by: generating or purchasing the necessary power; purchasing federally tariffed transmission service from the local utility (and potentially other utilities as well) to carry the power in bulk; purchasing distribution service from the local utility to deliver the power; and selling the power in a state-regulated retail transaction. The consumer would choose between energy suppliers based on the price and quality of their delivered power.

transmission to an ultimate consumer. 1 J.A. 350.[11] The Commission explained that its jurisdiction attaches only if the utility provides unbundled transmission in interstate commerce for energy sold at retail. *Ibid.* Therefore, a utility need not file a federal tariff for transmission in connection with retail sales unless it is ordered by the State to provide such transmission, or it offers that service voluntarily. *Ibid.*

The Commission observed that its jurisdiction over the rates, terms, and conditions of unbundled transmission would not affect the States' authority to regulate matters traditionally within their jurisdiction, such as the siting of public utilities' facilities, standards for local service reliability, and the availability of local retail electric service. 1 J.A. 351-353 & nn. 543, 544. Jurisdiction over such matters remains with the States, which "have jurisdiction in all circumstances over the service of delivering energy to end users." 1 J.A. 355.

c. In Order No. 888-A (excerpted at 2 Pet. App. 371a-551a and 2 J.A. 517-791), the Commission addressed petitions for rehearing of Order No. 888 and reaffirmed and clarified its jurisdictional holdings. See 2 Pet. App. 453a-456a; 2 J.A. 580-611. The Commission rejected the argument that, by asserting jurisdiction over all unbundled transmission in interstate commerce, it was "taking away" state jurisdiction over transmission in connection with retail sales. In the Commission's view, "[t]he fact that states historically regulated most retail transmission service as a part of a bundled retail power sale is * * * the practical result of the way electricity has historically been bought and sold," but power markets are "rapidly changing." 2 J.A. 593. The Commission explained that it was not intruding upon the States' historical jurisdiction, but rather applying the FPA

[11] Section 212(h)(1) prohibits the Commission from issuing orders that are "conditioned upon or require the transmission of electric energy * * * directly to an ultimate consumer." 16 U.S.C. 824k(h)(1).

to a new paradigm—not specifically contemplated by Congress in 1935—in which transmission service is provided in a transaction that is separate from the retail sale of energy, and sometimes by a separate provider. In "[t]oday's unbundled world," the Commission concluded, the States' jurisdiction over retail sales of electric energy does not necessarily include jurisdiction over associated transmission. 2 J.A. 593-595.

5. The court of appeals affirmed Orders No. 888 and 888-A in all relevant respects. 1 Pet. App. 3a-121a. In particular, the court rejected arguments by some States that the Commission asserted too much jurisdiction over unbundled transactions, and from some industry members that the Commission asserted too little jurisdiction over bundled transactions. *Id.* at 27a-35a.

The state petitioners argued that Section 201 of the FPA gives the Commission authority to regulate transmission of electric energy only when the energy is consumed in a State other than the one in which it was generated, and only when the transmission has not historically been regulated by the States. They therefore maintained that the Commission exceeded its statutory authority by exercising jurisdiction over the transmission component of unbundled retail power transactions in interstate commerce. 1 Pet. App. 30a.

Addressing those arguments, the court observed that "[b]oth FPA § 201(a) and (b) clearly and unambiguously confer upon [the Commission] jurisdiction over the 'transmission of electric energy in interstate commerce.'" 1 Pet. App. 32a. Furthermore, the court of appeals explained, in *Jersey Central Power & Light Co.* v. *FPC*, 319 U.S. 61 (1943), and *FPC* v. *Florida Power & Light Co.*, 404 U.S. 453 (1972), this Court upheld assertions of federal jurisdiction over public utilities based upon their interstate interconnection and the resulting energy flows. 1 Pet. App. 32a-34a. Following those decisions, the court of appeals "conclude[d] that the FPA gives [the Commission] the authority

to regulate [the unbundled] transmissions at issue here, whether retail or wholesale." *Id.* at 34a. In the alternative, and even if this Court's decisions and the text of the FPA did not clearly compel the Commission's assertion of jurisdiction over the interstate transmission component of unbundled retail transactions, the court stated that it would be "hard pressed" to find the Commission's construction of the FPA "unreasonable or impermissible," and, accordingly, the court would defer to the Commission's construction under *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984). 1 Pet. App. 35a.

The court of appeals also rejected the private petitioners' arguments that the Commission erred by not asserting jurisdiction over transmission in bundled as well as unbundled retail transactions, and, in doing so, subjecting retail service that currently is bundled to the rates, terms, and conditions of the pro forma open-access tariff set out in Order No. 888. 1 Pet. App. 30a-31a, 35a. The court explained that Section 201 of the FPA clearly establishes federal jurisdiction over transmission, and clearly preserves state jurisdiction over local distribution facilities and retail sales, but "[t]he statute is much less clear about exactly where the lines between those activities are to be drawn." *Id.* at 35a. In the court's view, "[a] regulator could reasonably construe transmissions bundled with generation and delivery services and sold to a consumer for a single charge as either transmission services in interstate commerce or as an integral component of a retail sale." *Ibid.* The Commission's decision to treat the transmission component of bundled retail sales as part of the retail sale of energy therefore "represents a statutorily permissible policy choice to which we must also defer under *Chevron*." *Ibid.*

The court of appeals next upheld, against challenge by the petitioner States, the Commission's exercise of exclusive jurisdiction over the transmission of power to a wholesale purchaser, to the extent it occurs over facilities that would

be state-regulated "local distribution" facilities in the context of a retail transaction. 1 Pet. App. 35a-39a. The court determined that Section 201 "makes clear that all aspects of wholesale sales," including associated transmission and transmission facilities, "are subject to federal regulation, regardless of the facilities used." *Id.* at 38a.

Finally, the court of appeals upheld the Commission's approach to distinguishing local distribution facilities from transmission facilities in the context of unbundled retail transactions. 1 Pet. App. 39a. The court pointed out that while Section 201(b)(1) assigns the States jurisdiction over "facilities used in local distribution," Congress did not define this statutory phrase. *Ibid.* Because the Commission's multi-factor approach to interpreting and applying "undefined and ambiguous" statutory language was reasonable, the court concluded that it warrants *Chevron* deference. *Ibid.*

SUMMARY OF ARGUMENT

I. A. Section 201(b)(1) of the FPA authorizes the Commission to regulate "the transmission of electric energy in interstate commerce." 16 U.S.C. 824(b)(1). Because electric energy "commingles" in interconnected power systems without regard to its source or the ultimate user of the energy, see *FPC* v. *Florida Power & Light Co.*, 404 U.S. 453, 463 (1972), Congress's express grant of authority over interstate transmission allows the Commission to regulate all transmission over power systems that are connected to an interstate power grid. New York never asked the Commission to consider its factual argument that the electric energy of a particular generating station is used only by those consumers nearest to the station, and that argument is inconsistent with the analysis uniformly applied in prior precedent.

B. New York's claim that federal jurisdiction over interstate transmission extends only to transmission associated

with wholesale sales of energy likewise conflicts with the text of Section 201(b). Whereas Congress expressly confined the Commission's jurisdiction over *sales* of energy in interstate commerce to wholesale sales, the Commission's jurisdiction over interstate *transmission* is not similarly qualified. This Court's interpretation of the analogous jurisdictional provision of the Natural Gas Act, 15 U.S.C. 717(b), confirms that the Commission's jurisdiction over interstate transmission is in addition to, and is not limited by, its jurisdiction over wholesale sales of energy. *FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972).

The FPA does reserve jurisdiction over non-wholesale sales of energy, and over facilities used in the local distribution of energy, to the States. But those carve-outs from federal jurisdiction do not limit the Commission's jurisdiction over interstate transmission services.

C. Congress's declaration of policy in Section 201(a) of the FPA, 16 U.S.C. 824(a), further confirms that the Commission has jurisdiction over wholesale sales of energy and, separately, over interstate transmission of energy (whether for wholesale or retail sales). Although New York relies heavily on the FPA's legislative history to support its contrary argument, New York has not identified a single statement that the States would regulate interstate transmission if such transmission were offered separately from electric energy and consumers had a choice of energy suppliers. Because the legislators who drafted the FPA deemed vertically integrated public utilities to be natural monopolies, they did not contemplate the provision of transmission service for retail transactions separately from retail sales of energy.

Relying on cases addressing federal preemption of traditional state regulation, New York argues that because Congress did not contemplate unbundled transmission in connection with retail sales of energy, it did not make a sufficiently clear assertion of federal jurisdiction over that

service. The absence of any historical tradition of state regulation of the new service of unbundled transmission for retail transactions renders inapposite the cases on which New York relies. In any event, Section 201(b)(1) does unequivocally assign the Commission jurisdiction over "the transmission of electric energy in interstate commerce." 16 U.S.C. 824(b)(1).

D. Order No. 888 leaves traditional state regulation undisturbed. The Commission explained in Order No. 888 that its rules would not divest the States of jurisdiction over retail sales of electric energy or local distribution facilities, and that the States retain jurisdiction over other local matters such as power production, siting of facilities, customer service, and local service reliability. The current energy crisis in California, moreover, does not support New York's policy arguments against Order No. 888. That situation involves supply and demand factors and rules governing power markets that are unrelated to the allocation of jurisdiction over unbundled transmission service.

II. Although Congress clearly intended to assign the Commission jurisdiction over transmission in interstate commerce when that transmission is separate from a sale of electric energy, nothing in the FPA clearly resolves the question of whether—in a market where energy can potentially be purchased from suppliers other than the traditional local utility—a public utility's bundled retail sale of energy and associated transmission should be treated as a single transaction subject to state regulation, or, instead, as both a transmission transaction subject to federal regulation and a retail sale of energy subject to state regulation. The Commission reasonably resolved that ambiguity in the statute by adhering to 65 years of practice under the FPA, and holding that transmission provided as part of a bundled retail sale of electric energy is subject to state jurisdiction.

ARGUMENT

Under the Commission's jurisdictional holding, traditional state regulation is not disturbed, but the Commission is able to apply its open-access tariff rules uniformly to all unbundled interstate transmission, thus preventing public utilities from abusing their control over the transmission facilities that are needed to support competitive power markets. Wholesale customers, and retail customers in States that have authorized competition in the retail market, can be served over interstate transmission grids on a nondiscriminatory basis, giving them a meaningful opportunity to consider alternative suppliers. But when an incumbent utility operates as a traditional monopoly utility and sells generation, transmission, and distribution to the consumer in a bundled package, the State will continue to regulate that bundled retail service. The Commission's interpretation and application of the FPA in these circumstances establishes a sound and workable regulatory framework that fully complies with the text of the Federal Power Act and the underlying legislative intent.

I. THE COMMISSION CORRECTLY INTERPRETED THE FEDERAL POWER ACT AS ESTABLISHING FEDERAL JURISDICTION OVER UNBUNDLED TRANSMISSION OF ELECTRIC ENERGY IN INTERSTATE COMMERCE

New York, as petitioner in No. 00-568, argues that the Commission is "attempting to preempt" (N.Y. Pet. Br. 10) state jurisdiction over transmission that historically has been regulated by the States, and that the FPA precludes federal regulation of any aspect of retail service. Those arguments are incorrect.

A. Transmission By A Utility That Utilizes An Interstate Grid Is "In Interstate Commerce"

The plain language of Section 201(b)(1) of the FPA establishes federal jurisdiction over "the transmission of electric energy in interstate commerce" and "all facilities for such transmission," but excludes from the Commission's jurisdiction "facilities used * * * only for the transmission of electric energy in intrastate commerce." 16 U.S.C. 824(b)(1). Section 201(c) provides that "electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof," but within the United States. 16 U.S.C. 824(c). Therefore, subject to exclusions that preserve state jurisdiction over retail sales of energy and over local distribution facilities (which we discuss in Part I.B., below), Congress vested the Commission with jurisdiction over all transmission of electric energy that involves origination and consumption in different States, and over all the facilities used for such transmission. That express conferral of authority on the Commission defeats New York's claim of state jurisdiction.

1. New York argues (N.Y. Pet. Br. 36-37, 43-46) that Section 201(b)'s textually broad assignment of jurisdiction over interstate transmission to the Commission is illusory, because the Commission may not exercise jurisdiction over a public utility's transmission service under that provision unless it "show[s] that essentially every electron used by a retail customer in each state [served by the utility] * * * is generated in a different state" (*id.* at 45 n.27). This Court's decisions foreclose New York's exceedingly narrow view of the Commission's transmission jurisdiction and establish the very different rule that when utilities connect their facilities to an interstate grid, their electricity presumptively flows "in interstate commerce" for purposes of Section 201. See 1 J.A. 389 ("[T]he highly integrated nature of the electric

system * * * results in most transmission of electric energy being 'in interstate commerce.'").

In *Connecticut Light & Power Co.* v. *FPC*, 324 U.S. 515 (1945), the Court explained that the "[t]echnology of the business is such that if any part of a supply of electric energy comes from outside of a state it is, or may be, present in every connected distribution facility." *Id.* at 529. Accordingly, the Court observed in *Arkansas Electric Cooperative Corp.* v. *Arkansas Public Service Commission*, 461 U.S. 375, 381 (1983), that when a utility is "ultimately tied into a multicompany and multistate 'grid,' * * * it is difficult to say with any confidence that the power [the utility] provides to its [customers] at any particular moment originated entirely within the State." See also *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 336 (1982) (when the utility is connected to a regional transmission network, it is "impossible to contain" power generated by the utility within the State where it is generated).

A utility might attempt to take extraordinary measures to isolate its operations from interstate transmission. In *Connecticut Light & Power*, for example, federal jurisdiction was put in doubt when "the [utility] rearranged its operations with intent to cut every connection and discontinue every facility whose continued operation would render it subject to the Federal Power Commission's control." 324 U.S. at 518-519. But such a quarantine from the interstate grid must be complete to be effective for jurisdictional purposes. In *Jersey Central Power & Light Co.* v. *FPC*, 319 U.S. 61 (1943), Jersey Central was deemed to use its facilities "for the transmission of electric energy across state lines" even though it had no direct connection to any utility outside New Jersey, on the ground that one of Jersey Central's in-state customers exchanged power (some of which came from Jersey Central) with a New York company. *Id.* at 63-67. Similarly, in *FPC* v. *Florida Power & Light Co.*, 404 U.S. 453 (1972), Florida Power was "unusually insular

and independent" as a result of Florida's "peninsular nature" and the risk of hurricane damage to transmission lines. But although Florida Power had no direct connection with any out-of-state utility, it did connect with an adjacent Florida utility that, in turn, connected to a Georgia utility and an interstate power grid. *Id.* at 456-457. The Court held that Florida Power transmitted electricity in interstate commerce if any of its power reached the Georgia company, or vice-versa, "no matter how small the quantity." *Id.* at 454-455, 458, 461 n.10. Because Florida Power's energy "commingled" with the Georgia company's energy by virtue of the connection through the second Florida utility, this Court held that Florida Power transmitted energy in interstate commerce and was subject to the Commission's jurisdiction. *Id.* at 458, 461, 463.

New York asserts (N.Y. Pet. Br. 37-39, 40, 43-44) that *Jersey Central* and *Florida Power* addressed only the question of whether the public utility itself was subject to Commission jurisdiction, and did not hold that every transmission of electricity by an interconnected utility is subject to federal regulation. New York further suggests that considering transmissions to be "in interstate commerce" on the basis that the utility is connected to an interstate grid renders Section 201(c) of the FPA "[n]early [n]ugatory," because virtually all transmission would be across state lines. *Id.* at 44-45.

New York ignores that the Commission's open-access requirements apply only to "unbundled transmission *in interstate commerce*." 1 J.A. 384 (emphasis added); see 2 J.A. 597 (Order No. 888-A) (asserting jurisdiction over "retail wheeling in interstate commerce that is ordered by a state or that is provided voluntarily"). The Commission acknowledged that it has no jurisdiction under Sections 205 and 206 of the FPA over unbundled retail transmission in Alaska, Hawaii, and much of Texas, "since transactions in those areas are intrastate." 1 J.A. 349 n.541. In theory,

moreover, any public utility could attempt to show that particular transmissions involve exclusively intrastate energy. Cf. *Florida Power*, 404 U.S. at 457 n.8, 469 (discussing "tracing studies" and expert testimony used to establish federal jurisdiction); N.Y. Pet. Br. 45 n.28 (noting the theoretical possibility of closed, "radial" transmission systems).

The important point for present purposes, however, is the practical reality that physically isolated utilities "have become a thing of the past." 2 Pet. App. 585a. As utilities have connected to interstate networks, their electric energy has commingled with other energy in the networks, "just as molecules of water from different sources (rains, streams, etc.) would be commingled in a reservoir." *Florida Power*, 404 U.S. at 461. Consequently, the energy the interconnected utilities sell from the interstate grids is in interstate commerce. See *ibid.*; cf. *California* v. *Lo-Vaca Gathering Co.*, 379 U.S. 366 (1965) (commingling of natural gas within Commission jurisdiction with gas outside of Commission's jurisdiction establishes Commission jurisdiction over all of the gas). Even New York's amicus recognizes that fact. Cal. Br. 11 ("[W]hen any part of the electricity moves across state lines, transmission all the way to the retail customer is transmission in interstate commerce.").

The overwhelmingly interstate nature of electrical transmission therefore has to do with the evolution of electric power systems, not Order No. 888. Indeed, Congress was well aware in 1935 that the Act gave the FPC broad jurisdiction over interconnected utilities and their transmission services.[12]

---

[12] See S. Rep. No. 621, 74th Cong., 1st Sess., Pt. 2, at 5 (1935) (minority views) (stating that, because "it is almost always impossible to separate * * * transmission facilities between those used only for energy sold interstate and energy sold intrastate," the FPA would cause "almost complete displacement of State jurisdiction over electric utilities"); 00-568 Pet. App. L-35 to L-36 (testimony of FPC Solicitor DeVane that the draft legislation "gives the Commission control over interstate transmission facilities" and that, "not withstanding 90 percent of the business is intrastate and 10 percent is interstate, this bill gives [the FPC] the power to regulate"); *Public Utilities Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce*, 74th Cong., 1st Sess., Pt. 2, at 241 (1935) (testimony of Solicitor DeVane that interconnection between power systems "would tend to greatly increase the percentage" of power transferred across state lines); Enron Pet. Br. 30 n.20 (quoting House committee hearings). In *Florida Power*, Justice Douglas stated in dissent that, in light of the Court's holding, "every privately owned interconnected facility in the United States (except for those isolated in Texas) is within the FPC's jurisdiction." 404 U.S. at 471.

New York concedes that the view "that all transactions affect the entire grid * * * is arguably accurate, from a theoretical standpoint" (N.Y. Resp. Br. 25), but nevertheless suggests that "[m]ost electricity used in the United States is generated in the state where it is used" (N.Y. Pet. Br. 5). See also *id.* at 45 n.28; N.Y. Resp. Br. 25-26. That argument echoes an argument this Court implicitly rejected in *Florida Power*. See 404 U.S. at 462 (noting Florida Power's argument that "all of [its] power will be exhausted * * * before the point, further down the line, where Georgia's load intervenes"); *id.* at 469 (upholding Commission finding that energy traveled across the Florida border). New York, moreover, did not present its factual claims about network operations to the Commission or to the court of appeals, and they therefore are not properly before this Court. See *FPC* v. *Sunray DX Oil Co.*, 391 U.S. 9, 36 n.21 (1968); *Glover* v. *United States*, 121 S. Ct. 696, 701 (2001); see also 16 U.S.C. 825*l*(b) (barring judicial review of claims not raised in petition for rehearing). In any event, even if a particular utility could show that its transmission service involves *mostly* intrastate energy, that would not defeat federal jurisdiction, for "Congress has not 'conditioned the jurisdiction of the Commission upon any particular volume or proportion of

interstate energy involved.'" *Florida Power*, 404 U.S. at 461 n.10 (quoting *Connecticut Light & Power*, 324 U.S. at 536). Indeed, under the express terms of Section 201(b)(1), transmission facilities (other than local distribution facilities) are within the Commission's jurisdiction unless they are used "*only* for the transmission of electric energy in intrastate commerce." 16 U.S.C. 824(b)(1) (emphasis added).

B. Congress Did Not Exclude Unbundled Retail Transmission From The Commission's Jurisdiction Over Interstate Transmission

1. New York further argues (N.Y. Pet. Br. 30-31) that the Commission's jurisdiction over interstate transmission is limited to transmission provided in connection with wholesale transactions.[13] Section 201(b)(1), however, states that "[t]he provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. 824(b)(1). As the court of appeals held, that plain language "clearly and unambiguously confer[s] upon [the Commission] jurisdiction over the 'transmission of electric energy in interstate commerce,'" *in addition to* "the sale of electric energy at wholesale in interstate commerce." 1 Pet. App. 32a, 34a.

Decisions under the Natural Gas Act of 1938, 15 U.S.C. 717 *et seq.*, confirm that the Commission's jurisdiction over wholesale sales of energy *supplements* the Commission's jurisdiction over transmission, rather than limiting that jurisdiction. See 2 J.A. 420-425. Because large portions of

[13] That argument is outside the scope of the question on which this Court granted certiorari. See Sup. Ct. R. 14(1)(a). Question 1 of New York's petition in No. 00-568, on which this Court granted certiorari, raised only the question of the Commission's power to assert jurisdiction over "*intrastute* retail transmissions of electric energy" transmitted "from generators to retail customers in the same state." New York Pet. i (emphasis added).

the Natural Gas Act "are in all material respects substantially identical" to the FPA, this Court "cit[es] interchangeably decisions interpreting the pertinent sections of the two statutes." *Arkansas La. Gas Co.* v. *Hall*, 453 U.S. 571, 577 n.7 (1981). Moreover, as with the FPA, the Natural Gas Act was drafted in a time of bundled retail sales. See 1 J.A. 347, 422.[14] Section 1(b) of the Natural Gas Act, which is relevant here, closely tracks Section 201(b) of the FPA: Commission jurisdiction extends to "the transportation of natural gas in interstate commerce, [and] to the sale in interstate commerce of natural gas for resale," but "not * * * to any other transportation or sale of natural gas or to the local distribution of natural gas, or to the facilities used for such distribution." 15 U.S.C. 717(b). In *FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621 (1972), the Court explained that Section 1(b) establishes federal jurisdiction over: "(1) the transportation of natural gas in interstate commerce; (2) its sale in interstate commerce for resale; and (3) natural gas companies engaged in such transportation or sale." *Id.* at 636 (quoting *Panhandle E. Pipeline Co.* v. *Public Serv. Comm'n*, 332 U.S. 507, 516 (1947)). Accordingly, the Natural Gas Act "applies to interstate 'transportation' regardless of whether the gas transported is ultimately sold retail or wholesale." *Ibid.* (quoting *FPC* v. *East Ohio Gas Co.*, 338 U.S. 464, 468 (1950)); see *id.* at 637-638. New York's argument that the Commission has jurisdiction over interstate transmission under the FPA only if the electric energy being transmitted is sold at wholesale fails under a parallel analysis.

[14] As under the FPA, the Commission has implemented an open-access program under the Natural Gas Act. That program is similar in many respects to the open-access program established by Order No. 888. See generally *United Distribution Cos.* v. *FERC*, 88 F.3d 1105 (D.C. Cir. 1996) (addressing jurisdictional and other challenges to open-access program under Natural Gas Act).

2. The Commission recognized (see generally 1 J.A. 384-430) that Congress, having established in Section 201(b)(1) "broad" federal jurisdiction over interstate transmission, wholesale sales, and facilities for such transmission and sales, then imposed specific limits on the reach of that grant in order "to respect state rights and local institutions." *Connecticut Light & Power*, 324 U.S. at 530. As relevant here, Congress carved out from the Commission's sphere, and reserved to the States, jurisdiction over (1) "any other sale of electric energy" and (2) "facilities used in local distribution." 16 U.S.C. 824(b)(1). Neither of those exclusions denies the Commission the authority to regulate unbundled interstate transmission in connection with retail sales.

a. *"Any Other Sale of Energy."* New York does not suggest that transmission in connection with retail sales is an "other sale of electric energy" for purposes of Section 201(b)(1). That reservation of state jurisdiction refers back to Congress's assertion, earlier in Section 201(b)(1), of federal jurisdiction over "the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. 824(b)(1). Together, those two provisions establish the "bright line" between wholesale and retail sales of which this Court has spoken. *Colton*, 376 U.S. at 215; see S. Rep. No. 621, 74th Cong., 1st Sess., Pt. 1, at 48 (1935) (noting that Section 201(b) establishes federal jurisdiction over wholesale sales but not retail sales). The "sales" provisions simply do not address the Commission's jurisdiction over transmission. Transmission consists of transporting energy in bulk from generating stations, typically to the local distribution facilities that serve most end users; although transmission service may be sold with energy on a bundled basis, transmission is not itself a sale of energy. See 1 J.A. 349-350, 387-388.

b. *"Facilities Used In Local Distribution."* The Commission identified seven indicators that will guide its determination whether particular facilities of a public utility are transmission facilities subject to federal jurisdiction, or,

alternatively, local distribution facilities subject exclusively to state jurisdiction when used in connection with a retail sale of energy. See 1 J.A. 425-430. Without challenging the specifics of that test, California suggests (Br. 7-17) that, when Congress assigned jurisdiction over "facilities used in local distribution" to the States, it disclaimed federal regulation of each and every facility, including transmission facilities, that supports retail electric service. See also N.Y. Pet. Br. 31-33.

California's theory cannot be reconciled with the text of Section 201(b)(1). As discussed above, that section limits the Commission's jurisdiction over interstate sales of energy to sales "at wholesale," but does not similarly limit the Commission's jurisdiction over interstate transmission and transmission facilities. 16 U.S.C. 824(b)(1). If Congress had intended to limit the Commission's transmission jurisdiction to transmission in connection with wholesale sales, it would have done so explicitly, just as it did when limiting the Commission's sales jurisdiction to wholesale transactions. Congress would not have hidden its intent regarding transmission service associated with retail sales in a reference to "facilities used in local distribution." 16 U.S.C. 824(b)(1).[15]

California's argument that all facilities used to provide transmission in connection with retail sales are "used in local distribution" also is contrary to industry usage of the term "distribution," which refers to lower-voltage circuits that provide electricity to customers over relatively short distances. Compare H. Rustebakke, *supra*, at 122 (defining "transmission") with *id.* at 199 (defining "distribution sys-

[15] If Congress had intended to limit the Commission's transmission jurisdiction as California suggests, it logically would have begun Section 201(b) by saying something like: "The provisions of this subchapter shall apply to the sale of electric energy at wholesale in interstate commerce and to the transmission of electric energy in interstate commerce for such sales * * * ."

tem"). Indeed, legislative history that New York quotes selectively (N.Y. Pet. Br. 33), when read in full, confirms that Congress drew a jurisdictional line based on the physical distinction between transmission systems and local distribution facilities. See 00-568 Pet. App. L-32 (testimony of FPC Solicitor DeVane that "[t]he bill does not give the Commission any jurisdiction whatever over facilities used in local distribution or the transmission facilities that are used in connection with such local distribution, *unless they are also a part of the facilities that are used in interstate commerce.*") (emphasis added).

This Court's cases also foreclose California's claim that transmission facilities used for retail sales are local distribution facilities. In *Connecticut Light & Power*, the Court reviewed an FPC determination that local distribution begins where "the function of conveyance in bulk over a distance, which is the essential characteristic of 'transmission,' is completed and the process of subdividing the energy to serve ultimate consumers * * * is begun." 324 U.S. at 533 (quoting FPC order). Although the Court found the FPC's rationale for its jurisdictional line insufficient, both the majority and the dissenting Justices agreed with the FPC that distinguishing transmission facilities from facilities used in local distribution was a matter of identifying an "exact point" of demarcation in the network. *Id.* at 534, 539, 541. Similarly, the Court held in *Colton* that deciding whether facilities are used in local distribution implicates "the specialized experience of the FPC in determining such questions." 376 U.S. at 210 n.6. Neither case suggests that a facility is "local" simply because it is used in connection with a retail transaction.

FPC v. *East Ohio Gas Co.* likewise undermines California's theory that the retail or wholesale nature of the sale of energy determines whether facilities are used in local distribution. The natural gas company in that case sold gas recovered from wells in various States, but the company had

facilities only in Ohio and sold its gas only at retail within Ohio. 338 U.S. at 467-468. The company argued that all of its facilities were local distribution facilities subject to exclusive state jurisdiction under Section 1(b) of the Natural Gas Act, 15 U.S.C. 717(b). 338 U.S. 468-469. The Court rejected that argument, holding that federal jurisdiction extends to the transportation of gas in interstate commerce through high-pressure transmission lines for delivery to retail customers, and that local distribution does not begin until the point where the gas enters local mains. *Id.* at 468-470. The fact that the company sold "direct to consumers rather than for resale" was "immaterial." *Id.* at 473.

Contrary to California's contention (Br. 24-25), *East Ohio* remains good law. In *Louisiana Power & Light*, the Court explicitly relied upon *East Ohio*'s jurisdictional analysis and quoted it at length. 406 U.S. at 636-637 & n.13. And *East Ohio* has been "repudiated" (Cal. Br. 24) only in the sense that Congress later amended the Natural Gas Act by adding a new provision that effectively overturned *East Ohio* in the natural gas context. See *General Motors Corp.* v. *Tracy*, 519 U.S. 278, 293 (1997). Congress has never made a parallel amendment to the FPA.[16] Finally, there is no inconsistency between the rule of *East Ohio* and *Pennsylvania Gas Co.* v. *Public Service Commission*, 252 U.S. 23 (1920). See Cal. Br. 9-10, 24-25. *Pennsylvania Gas*, which predates both the FPA and the Natural Gas Act, stands for the proposition that "the furnishing of natural gas to local consumers within [a] city" is local service subject to state regulation. 252 U.S.

---

[16] The so-called "Hinshaw Amendment" added a new Section 1(c), 15 U.S.C. 717(c), to the Natural Gas Act. Section 1(c) provides, among other things, that facilities used in the transportation of natural gas in interstate commerce, or in the sale of natural gas in interstate commerce for resale, are exempt from the Commission's jurisdiction if the gas is received within or at the boundary of a State and is consumed within the State, and if the State has asserted jurisdiction. New York is, in effect, asking this Court to write a similar amendment into the FPA.

at 31. Consistent with that principle, Order No. 888 reaffirmed that the States have jurisdiction over sales of energy to retail customers. See 1 J.A. 349-350.

C. The Commission's Jurisdictional Holding Is Consistent With Congress's Purposes In Enacting Section 201

1. New York places great weight on Section 201(a) of the FPA, which "declare[s] * * * that Federal regulation * * * of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States." 16 U.S.C. 824(a); see N.Y. Pet. Br. 16, 18-26, 27-28, 30-34.

Congress's declaration of policy does not trump the specific jurisdictional rules set out in Section 201(b). In *FPC* v. *Southern Cal. Edison Co.*, 376 U.S. 205 (1964), the Court explained that whereas "Section 201(b) embodies a clear grant of power," Section 201(a) is "merely a 'policy declaration . . . of great generality'" that "cannot nullify a clear and specific grant of jurisdiction, even if the particular grant seems inconsistent with the broadly expressed purpose." *Id.* at 215 (quoting *Connecticut Light & Power*, 324 U.S. at 527).

In any event, Section 201(a) states the same rule as Section 201(b): the Commission has jurisdiction over wholesale sales of energy in interstate commerce and, independently, over the transmission of energy in interstate commerce. Even if Section 201(a)'s "ambiguous reference to 'matters . . . subject to regulation by the States'" (*United States* v. *Pub. Utils. Comm'n (California PUC)*, 345 U.S. 295, 308-309 (1953)) were read as covering all matters that traditionally have been regulated by the States (see N.Y. Pet. Br. 27-28), that would not help New York. The States have *not* traditionally regulated unbundled interstate transmission associated with retail sales.

In that regard, it is important to emphasize the fallacy of New York's repeated assertions (N.Y. Pet. Br. 8-9, 27, 35) that the only difference between today's unbundled transmission and the bundled retail service that Congress had in mind in 1935 "is a change in bill format." *Id.* at 8; see also Enron Br. 18, 37. As used in Order No. 888, "unbundling" is one aspect of the Commission's broader concept of "open access," under which public utilities are required to provide nondiscriminatory access to their transmission systems so that purchasers of power have a meaningful opportunity to obtain power across the grid from alternative suppliers. 1 J.A. 50-52, 106. The Commission has not asserted jurisdiction over unbundled retail transmission simply because a public utility *bills* its retail customers separately for generation and transmission. Rather, the Commission's open-access tariff and its jurisdiction over rates, terms, and conditions of interstate transmission in connection with retail sales apply when the traditional, bundled transaction "is broken into two products that are sold separately (perhaps by two different suppliers: an electric energy supplier and a transmission supplier)," and the customer can choose an energy supplier. 1 J.A. 349-350; see 2 J.A. 593-594. The defining difference between bundled retail service and unbundled services is the customer's opportunity to choose a different power supplier if the local public utility fails to offer a competitive price and quality of service. And as the Commission recognized, that opportunity to choose is not meaningful unless alternative suppliers have access to essential transmission facilities on nondiscriminatory terms and conditions. 2 Pet. App. 558a.

New York also suggests (N.Y. Pet. Br. 24 n.12, 36, 40) that Section 206(d) of the FPA, 16 U.S.C. 824e(d), shows that Congress did not intend to give the Commission jurisdiction to set rates for any services associated with retail sales of energy. See also Cal. Br. 17-18. Section 206(d) authorizes the Commission to "investigate and determine the cost of the

production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy." 16 U.S.C. 824e(d). That authority would be useful, for example, when a single public utility generates electric power in one State and sells it to retail customers in another State, or when a single utility's service area straddles a state line.[17] Consistent with Section 206(d), Order No. 888 respects the States' "authority to establish a rate governing the sale of * * * energy" (16 U.S.C. 824e(d)) in those interstate settings, even when the transmission service is unbundled from the retail sale of energy. Although the Commission would regulate rates for transmission service, the State would regulate the sale of energy, and, in connection with that state regulation, the Commission could provide information pursuant to Section 206(d) regarding production or transmission costs that are outside the State's jurisdiction. See 1 J.A. 354-355, 425-430.

New York further argues (N.Y. Pet. Br. 33-34, 36) that Section 212(h) of the FPA, 16 U.S.C. 824k(h), forecloses Commission jurisdiction over unbundled retail transmission services in interstate commerce. As the plain language of Section 212(h) states, and as the Commission explained in Order No. 888, that provision "prohibit[s the Commission] from *ordering* transmission directly to an ultimate consumer." 2 J.A. 596 (emphasis in original); see note 11, *supra*. The Commission respected that limitation by ordering public utilities to provide "functional unbundling" of transmission services only in the context of wholesale transactions. See 1 J.A. 106, 350. A public utility is not required to file a federal

[17] See H.R. Rep. No. 1318, 74th Cong., 1st Sess. 29 (1935) ("This subsection reaches those situations where electric energy is transmitted in interstate commerce by the same company which distributes it locally, and will greatly aid State commissions in fixing reasonable rates in such cases.").

tariff for unbundled interstate transmission in connection with retail sales unless the utility offers that transmission service voluntarily or state regulators—not federal regulators—allow retail competition by mandating the provision of such a transmission service. See 2 J.A. 695 (pro forma tariff § 1.11, limiting retail customers' eligibility for tariffed transmission service to customers served voluntarily or as part of a state retail access program).

2. The Act's legislative history, on which New York principally relies, is equally inconsistent with New York's theory of the case. The Senate Report on the Act states that Congress assigned the FPC jurisdiction over interstate transmission even "where there is no sale" of the energy being delivered. That statement confirms that the Commission's transmission jurisdiction is not limited to transmission accompanied by a wholesale sale of electric energy. S. Rep. No. 621, *supra*, Pt. 1, at 19; see also *id.* at 48 ("Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines").[18] Other legislative history is to the same effect. See Enron Pet. Br. 23-24.

[18] When Congress drafted the FPA, there already was a history of utilities providing transmission service for other utilities, without buying or selling the energy being transmitted. For example, in the *Attleboro* case, to which Congress responded when drafting the FPA, Seekonk Electric Company in Massachusetts received power generated in Rhode Island by Narragansett Electric Lighting Company, and carried that power over Seekonk's transmission lines to Attleboro Steam & Electric Company (also in Massachusetts), which had purchased the power from Narragansett. See *Attleboro Steam & Elec. Co.* v. *Public Utils. Comm'n*, 129 A. 495, 496 (R.I. 1925), aff'd, 273 U.S. 83 (1927).

California suggests that when the Senate committee said that Section 201 of the FPA gives the FPC jurisdiction over interstate transmission when there is no sale of energy, it actually meant that Section 206(d) allowed the FPC to provide accounting information to support the States' exercise of *their* jurisdiction in situations where there is a sale at retail but not at wholesale. Cal. Br. 17 & n.9. Even California seems not to take that

More generally, Congress intended to ensure that the FPC would be able to oversee those services and facilities that state regulators could not lawfully, or effectively, regulate. Congress's overriding concern was that there never be a jurisdictional void. See *Louisiana Power & Light*, 406 U.S. at 640-641; *Arkansas Elec. Coop.*, 461 U.S. at 384 ("Congress' purpose in 1935 was to fill a regulatory gap, not to perpetuate one."); S. Rep. No. 621, *supra*, Pt. 1, at 48.

New York's narrow reading of Section 201 would defeat that paramount legislative intent. If the State in which the retail customer is located has jurisdiction to regulate all unbundled transmission associated with a retail sale, there would be a large regulatory gap when the retail customer purchases power from a supplier in a distant State, and that supplier requires transmission service from intervening out-of-state utilities to deliver the power. See 1 J.A. 427. The intervening transmission would be beyond the jurisdictional reach of the consumer's State. Thus, under New York's theory, those out-of-state transmission services would not be subject to meaningful regulation.

The most important fact about New York's reliance on legislative history, however, is that New York is unable to identify any statement indicating an actual congressional intent that if interstate transmission were separated from the associated retail sale of energy, the unbundled transmission would be subject to exclusive state regulation. There is no such evidence, because "the legislative history of the FPA * * * grew out of a market structure in which electricity and transmission generally were bought and sold

---

strained reading of the Senate Report seriously, for it offers (*id.* at 17-18 n.10) two alternative theories. Like California's principal theory, however, both of the alternative theories implausibly assume that the Senate Report's discussion of federal transmission jurisdiction under Section 201(b) actually addressed the FPC's powers under entirely different, and unidentified, provisions of the Senate bill.

on a bundled basis." 1 J.A. 347. Accordingly, when legislators stressed that federal regulators would not "fix the rate of delivery" of electric power (see N.Y. Pet. Br. 24), and when the FPC noted that it lacked "authority over local rates" (see *id.* at 25-26), they were saying nothing more than what the Commission said in Order 888: Under the FPA, the States "clearly retain[] jurisdiction over" retail sales of power. 1 J.A. 350.[19]

3. New York admits (N.Y. Pet. Br. 12) that in 1935 Congress did not envision unbundling of retail transmission from retail sales of energy. But New York attempts to turn that fact to its advantage by arguing (*id.* at 13-17) that, as a matter of "preemption" law, the court of appeals in these cases erred by upholding the Commission's jurisdictional ruling absent "clear and manifest" Congressional intent regarding unbundled transmission. New York is mistaken on several counts.

First, New York's premise—that the Commission is seeking to seize jurisdiction over a service that the States traditionally have regulated (N.Y. Pet. Br. 14-15)—misstates the situation. Given that unbundled transmission in connection with retail sales is a new service, the Commission's task was not to decide whether historical state jurisdiction should

---

[19] Likewise, New York is mistaken when it says (N.Y. Pet. Br. 17) that the Commission has changed its interpretation of Section 201. The statements cited by New York (*id.* at 21-22, 25-26, 31 & n.14, 41, 42 n.26) simply, and consistently, acknowledge the States' jurisdiction over bundled retail sales and local distribution. They do not address jurisdiction over unbundled retail transmission in interstate commerce. In his Senate testimony, for example, FPC Solicitor DeVane distinguished the interstate wholesale sales that would be regulated by the FPC from "energy that is transmitted in interstate commerce by a particular company and sold by that company to consumers," which the States would continue to regulate. Mr. DeVane did not address any other potential retail arrangements. *Public Utilities Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce*, 74th Cong., 1st Sess., Pt. 2, at 250 (1935).

be "preempted," but to determine whether the new service comes within the States' unquestioned jurisdiction over bundled retail sales, or, rather, the Commission's clearly established jurisdiction over transmission in interstate commerce. See 2 J.A. 593-595; see generally *West* v. *Gibson*, 527 U.S. 212, 218 (1999) ("Words in statutes can enlarge or contract their scope as other changes, in law or in the world, require their application to new instances").

Second, the court of appeals' affirmance did not depend upon "the deferential standard of *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984)." N.Y. Pet. Br. 17 n.8.; see *id.* at 16. As the court of appeals stated, its primary holding was that the "clear[] and unambiguous[]" language of Section 201, as well as this Court's decisions in *Jersey Central* and *Florida Power*, compel the conclusion "that the FPA gives [the Commission] the authority to regulate transmissions at issue here, whether retail or wholesale." 1 Pet. App. 32a, 34a. *Chevron* deference was an alternative basis for upholding the Commission's jurisdiction. See *id.* at 34a-35a.[20]

Third, New York ignores *stare decisis* principles. Cases such as *Jersey Central*, *Connecticut Light & Power*, and *Florida Power* provide "cardinal and guiding" interpretations of Section 201 (*California* v. *FERC*, 495 U.S. 490, 497-499 (1990)), upon which the Commission properly relied. See *Maislin Indus., Inc.* v. *Primary Steel, Inc.*, 497 U.S. 116, 131 (1990) ("Once we have determined a statute's clear meaning, we adhere to that determination under the doctrine of *stare decisis*, and we judge an agency's later interpretation of the statute against our prior determination of the statute's meaning.").

[20] *Solid Waste Agency* v. *United States Army Corps of Engineers*, 121 S. Ct. 675 (2001), has no relevance even with respect to the court of appeals' alternative holding. See N.Y. Pet. Br. 16. In *Solid Waste Agency*, the Court declined to give *Chevron* deference to an agency interpretation that "push[ed] the limit of congressional authority" and therefore raised "significant constitutional questions." 121 S. Ct. at 683. In this case, the Court has already decided as a matter of constitutional law that "generation, transmission, distribution and consumption are so fused and interdependent that the whole enterprise is within the reach of the commerce power" if the utility connects to an interstate grid. *Connecticut Light & Power*, 324 U.S. at 529-530. The issue is whether, as a statutory matter, Congress chose to exercise its power to regulate unbundled retail transmission.

Fourth, New York disregards the presumption *in favor* of federal jurisdiction under Section 201, where such jurisdiction is necessary to fill a possible jurisdictional void. As noted above, "Congress desired regulation by federal authority rather than non-regulation." *Louisiana Power & Light*, 406 U.S. at 641 (citation and internal quotation marks omitted). Therefore, as this Court has held, the enumerated exceptions to federal jurisdiction stated in Section 201 "are to be strictly construed." *California PUC*, 345 U.S. at 310. New York's proposed approach of forbidding federal regulation unless there is affirmative evidence of congressional intent that the statutory exceptions will *not* apply, risks creating the very jurisdictional vacuum that Congress wanted to avoid.

In other cases that presented questions of federal jurisdiction under Part II of the FPA—such as *Jersey Central*, *Connecticut Light & Power*, and *Florida Power*—this Court has straightforwardly "construe[d] § 201(b) as it is written, and as its legislative history indicates it was intended," without applying the anti-federal gloss suggested by New York. *New England Power*, 455 U.S. at 343; see *Arkansas Elec. Coop.*, 461 U.S. at 379 (Part II of FPA "shifted this Court's main focus—in determining the permissible scope of state regulation of utilities—from the constitutional issues * * * to analyses of legislative intent."). The Court has taken the same approach when applying analogous jurisdictional provisions. See *Louisiana Pub. Serv. Comm'n* v. *FCC*, 476 U.S. 355, 359, 376-377 n.5

(1986) (treating resolution of conflict between federal and state telecommunications regulation as an ordinary matter of statutory interpretation). Contrary to New York's thesis, nothing in this Court's decisions suggests that the Commission or the court of appeals should have applied a presumption against federal jurisdiction.

D. Policy Considerations Also Do Not Support New York's Interpretation

Finally, New York argues (N.Y. Pet. Br. 46-48) that Order No. 888 will undermine the States' ability to ensure that consumers receive reliable retail electric service at just and reasonable rates. California similarly maintains (Br. 27-30) that the Commission lacks statutory authority to regulate unbundled retail transmission adequately, and that the Commission has made the wrong policy choices in the past.

Those policy arguments are "properly addressed to Congress, not to the Courts." *Chemehuevi Tribe of Indians* v. *FPC*, 420 U.S. 395, 423 (1975).[21] Furthermore, New York offers nothing to support its assertion that the Commission's regulation of unbundled retail transmission will hamper regulation of facilities and services within the States' jurisdiction. The Commission specifically clarified that, even if a State chooses to order retail unbundling, it retains authority under Order No. 888 over local matters such as power production, customer service, and local service reliability, in addition to its authority over rates for retail sales of energy. 1 J.A. 351-355. The Commission also committed—when exercising its jurisdiction over unbundled transmission in interstate commerce in connection with retail sales—to

[21] New York's invocation of *Chemehuevi Tribe* (N.Y. Pet. Br. 15) is wholly misplaced. In that case, the Court rejected an argument that statutory language should be disregarded when the policy choice underlying that language is outmoded. 420 U.S. at 422-424. Here, by contrast, the Commission applied the plain language of Section 201 to new circumstances.

cooperate with state regulators on various matters that implicate their expertise and concerns and to afford deference to the views of the States when applying its test for identifying local distribution facilities. 1 J.A. 355-360. Finally, while transmission assets may be shifted from state to federal jurisdiction as a result of retail unbundling, the resulting accounting issues would be "commonplace." *FPC* v. *Conway Corp.*, 426 U.S. 271, 280 & nn. 6, 7 (1976).

Nor is there merit to California's argument (Br. 28-29) that the Commission lacks the authority it needs to ensure adequate and nondiscriminatory transmission service. Order No. 888 requires public utilities to provide their unbundled transmission services to all eligible customers under the same terms and conditions that apply to the utility's own operations. See 2 J.A. 440-443 (18 C.F.R. 35.28(c), requiring public utilities to file open-access transmission tariffs and to obtain transmission service under those generally available tariffs). The Commission's pro forma tariff also obligates the public utility to take appropriate steps to provide sufficient transmission capacity to serve all tariff customers on a nondiscriminatory basis. 2 J.A. 729, 767-770 (tariff §§ 15.4, 32).

New York argues (N.Y. Pet. Br. 48) that Order No. 888 will deter States from requiring unbundling of transmission from retail sales, because unbundling would trigger federal jurisdiction and "diminish[]" the States' own jurisdiction over transmission. That contention assumes that States regulate to maximize their own jurisdiction, rather than to promote the public interest—a proposition New York itself rejects as respondent in No. 00-809. See N.Y. Resp. Br. 18-23. Indeed, numerous States have adopted "retail choice" programs since the Commission issued Order No. 888.[22]

[22] Before Order No. 888, 12 States had acted to give retail customers a choice of power suppliers. 1 J.A. 95 & n.101. As of May 2001, 25 States had adopted such programs by legislation or administrative order. See

California suggests (Br. 1) that the jurisdictional lines identified in Order No. 888 have contributed to that State's current energy crisis. Enron disagrees. Enron Resp. Br. 16 n.6. The Commission has found that the principal causes of California's electricity crisis were state regulations that required all utilities to purchase their wholesale requirements through a spot market exchange, froze retail rates at levels lower than wholesale rates, and inhibited construction of new electric generating capacity. *San Diego Gas & Elec. Co.* v. *Sellers of Energy and Ancillary Servs. into Mkts. Operated by the Cal. Indep. Sys. Operator and the Cal. Power Exch.*, 93 F.E.R.C. ¶ 61,121, at 61,351, 61,353, 61,360 (2000), mandamus denied, 245 F.3d 1110 (9th Cir. 2001). Those causal factors have nothing to do with regulation of unbundled transmission. Order No. 888 likewise does not implicate the disagreement regarding state control over the governing board of the California Independent System Operator, to which California refers (Br. 27-28). That disagreement, moreover, has been resolved. See *Western Power Trading Forum* v. *FERC*, 245 F.3d 798, 799-800 (D.C. Cir. 2001).

II. THE COMMISSION REASONABLY CONCLUDED THAT CONGRESS HAS NOT AUTHORIZED FEDERAL REGULATION OF THE TRANSMISSION COMPONENT OF BUNDLED RETAIL SALES OF ELECTRIC ENERGY

In No. 00-809, petitioner Enron, which supports the Commission's determination that the FPA establishes federal jurisdiction over *unbundled* transmission for retail sales, argues that the court of appeals erred by deferring to the Commission's further conclusion (1 J.A. 349-350) that it lacks jurisdiction to regulate the transmission provided by

---

Energy Information Administration, U.S. Dep't of Energy, *Status of State Electric Industry Restructuring Activity as of May 2001* (available at <http://www.eia.doe.gov/cneaf/electricity/chg_str/regmap.html>).

public utilities in their *bundled* retail sales. See 1 Pet. App. 35a. Enron contends (Enron Pet. Br. 21) that "Section 201(b) * * * explicitly gives [the Commission] jurisdiction, without any stated limitation or qualification, over all interstate transmissions * * * for both wholesale and retail sales," and that the Commission disregarded that "plain meaning" by "read[ing] into section 201(b) an exception for transmissions that are bundled at retail." Enron further suggests (*id.* at 41-43) that applying the Commission's pro forma open-access tariff to transmission that is bundled with a retail sale of energy is necessary to prevent public utilities from providing inferior transmission to transmission customers who do not also buy energy from the utility at retail.

Enron's understanding of the Commission's transmission jurisdiction is correct—as far as it goes. As the court of appeals held (1 Pet. App. 32a-34a), and as we have demonstrated in Part I, above, Section 201(b) assigns the Commission jurisdiction over interstate transmission whether it is used in conjunction with a wholesale sale of energy or a retail sale of energy. But Section 201(b)(1) also assigns the States jurisdiction over "any * * * sale of electric energy" that is not "at wholesale in interstate commerce." 16 U.S.C. 824(b)(1). The issue faced by the Commission, therefore, was whether a public utility's sale at retail of delivered energy in a single transaction—in a State that does not permit consumers to choose their power supplier—constitutes (1) a retail sale of energy within the States' jurisdiction, or (2) a state-regulated retail sale of energy *as well as* a federally regulated transmission service. See 1 J.A. 349-350.

The court of appeals correctly concluded (1 Pet. App. 34a) that "Congress has not directly addressed th[at] precise question" with unambiguous language. *Chevron U.S.A. Inc.* v. *Natural Res. Def. Council*, 467 U.S. 837, 843 (1984). Nothing in Section 201(b) establishes the proper characterization of a bundled transaction. Whereas Section 201(b) clearly gives the Commission jurisdiction over transmission,

and clearly gives the States jurisdiction over non-wholesale sales of energy, "[t]he statute is much less clear about exactly where the lines between those activities are to be drawn." 1 Pet. App. 35a.

Section 201(a) does not resolve the ambiguity. While federal jurisdiction "extend[s] only to those matters which are not subject to regulation by the States," 16 U.S.C. 824(a), that declaration of policy is, as this Court has held, itself ambiguous. *California PUC*, 345 U.S. at 308-309.

The legislative history of the FPA is inconclusive as well. Enron cites legislative history suggesting that the Act would give the Commission jurisdiction over interstate transmission "[w]hether it be wholesale or retail." Enron Pet. Br. 23 (quoting House hearings) (emphasis omitted); see *id.* at 23-24 (discussing legislative history). Other legislative history, however, reflects an intent to "tak[e] no authority from State commissions" and to maintain "valid state authority" that was then being exercised. *New England Power*, 455 U.S. at 341 & n.7 (emphasis omitted). In particular, the committee reports state that "the authority of States to fix local rates"—which then referred to bundled rates for delivered power, including the transmission component, see 2 J.A. 593-594—"[wa]s not disturbed." H.R. Rep. No. 1318, *supra*, 27; accord S. Rep. No. 621, *supra*, Pt. 1, at 48. Unlike the Commission's exercise of jurisdiction over the new service of unbundled retail transmission, the exercise of federal jurisdiction over the transmission component of traditional bundled retail service would affect historical state regulation and local rates.

Louisiana Power & Light also was not "controlling" (Enron Pet. Br. 22) on the record before the Commission in the Order No. 888 proceeding. The Court held in *Louisiana Power & Light* that the Commission had authority to direct interstate natural gas pipelines to curtail deliveries to all customers in time of shortage, and that such curtailment regulations did not interfere with the States' exclusive

authority over retail sales of gas. 406 U.S. at 623-647. The critical considerations under the Natural Gas Act were that curtailment rules did not implicate local rate-setting, *id.* at 637-638, and that leaving allocation of scarce gas to the States would "create contradictory regulations that cannot possibly be equitably resolved by the courts," *id.* at 634. Because the federal curtailment requirements addressed transportation rather than retail sales, *id.* at 638-640, and because state rationing of interstate gas was not feasible, *id.* at 641, the curtailment requirements were permissible.

Neither of those considerations was present on the record before the Commission in the Order No. 888 proceeding. Enron acknowledges (Enron Pet. Br. 26) that federal regulation of the transmission component of a bundled sale potentially implicates retail rate-setting. Furthermore, the record before the Commission did not establish that the current arrangement, under which the transmission component of bundled sales is subject to regulation as part of the regulation of retail sales, is unworkable. Cf. 1 J.A. 227 (finding that federal unbundling of retail transactions is not necessary to prevent discrimination), 2 Pet. App. 453a-454a (noting same).

Enron has never provided clear record support—in a rehearing petition before the Commission, in the court of appeals, or in this Court—for its argument (which the court of appeals did not address, see 1 Pet. App. 35a) that federal action with respect to the transmission component of a bundled retail sale is necessary to fill a gap created by practical limitations on state regulation. Nor has Enron shown that its proposal for a categorical extension of the open-access tariff requirement to bundled retail sales is necessary to ensure just, reasonable, and nondiscriminatory terms for services that *are* currently regulated by the Commission.[23]

---

[23] The Commission has concluded a rulemaking regarding Regional Transmission Organizations (RTOs) that addresses some of Enron's

Citing *Northern States Power Co.* v. *FERC*, 176 F.3d 1090 (8th Cir. 1999), cert. denied, 528 U.S. 1182 (2000), Enron suggests (Enron Pet. Br. 24-25 n.17, 42 & n.27) that, absent application of the open-access tariff to bundled retail transmission, public utilities facing a need to curtail their transmission will favor their own bundled retail service and disadvantage customers of unbundled transmission obtained under Order No. 888's open-access rules. In *Northern States Power*, the Commission had rejected proposed curtailment provisions of a public utility's federal open-access transmission tariff that favored the utility's retail customers over wholesale transmission customers who are unquestionably subject to the Commission's jurisdiction. The Eighth Circuit held that the Commission exceeded its authority under the Act. 176 F.3d at 1093-1096. While the Commission continues to believe that it has authority to require public utilities to treat customers of unbundled interstate transmission in a manner that is comparable to the treatment afforded bundled transmission users, and thereby to prevent discrimination against users of federally regulated services, the Commission has also concluded that even under the court of appeals' decision, it is not powerless to address such discrimination.[24]

concerns. Order No. 2000, *Regional Transmission Orgs.*, 65 Fed. Reg. 809, on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (2000), appeal pending *sub nom. Public Utils. Dist. No. 1* v. *FERC*, No. 00-1174 (D.C. Cir. to be argued Oct. 17, 2001). An RTO serves as the sole transmission provider within its region, providing all transmission for wholesale power transactions as well as bundled and unbundled retail power transactions. The Commission has provisionally approved three RTOs, and additional applications are pending. Also, Enron could in the future petition the Commission to revisit its resolution of the jurisdictional ambiguity in the FPA on the basis of changed industry conditions. See *Chevron*, 467 U.S. at 863-864.

[24] On remand from the court of appeals, the Commission recognized that a utility could depart from pro-rata transmission curtailment in the "rare circumstance[]" when the utility has exhausted all of its options for avoiding transmission curtailment, and has established that the transmission customers that would be disproportionately affected by the curtailment have options to reduce their need for transmission capacity. The Commission, however, required the utility to adopt specific tariff provisions for ensuring that all options for avoiding curtailment are first exhausted, and for affording those customers who would carry an extra burden either alternative supply options or compensation, as well as reduced rates for the inferior quality of service they are provided. *Northern States Power Co. (Minn.)*, 89 F.E.R.C. ¶ 61,178, at 61,553 (1999).

In light of the equivocal language and history of the FPA and the limited record before the Commission, the court of appeals properly deferred to the Commission's reasonable decision not to override the States' historical regulation of transmission that is bundled with a retail sale of energy. See generally *Chevron*, 467 U.S. at 842-845.[25] The Commission's jurisdictional determination, in turn, resolves Enron's final argument (Enron Pet. Br. 33-44) that Section 206 of the FPA, 16 U.S.C. 824e, requires the Commission to exercise jurisdiction over the transmission involved in public utilities' retail operations, even if the relevant State favors traditional bundled sales. Section 206 authorizes the Commission to remedy undue discrimination with respect to matters subject to its jurisdiction. See 16 U.S.C. 824e(a). In light of the Commission's reasonable finding that it lacks jurisdiction over the transmission component of bundled retail sales

[25] Enron relies on the supposedly "plain language of the statute" (Enron Pet. Br. 20; see *id.* at 43), and does not dispute that, if the statute and its legislative history are ambiguous, the Commission has provided a "reasonable interpretation" (*Chevron*, 467 U.S. at 844) of the FPA. Likewise, Enron does not challenge the court of appeals' holding (1 Pet. App. 34a-35a) that an agency's interpretation of a statutory provision that defines the scope of the agency's jurisdiction is entitled to *Chevron* deference. This Court has applied the same rule. See *CFTC* v. *Schor*, 478 U.S. 833, 844-845 (1986); *NLRB* v. *City Disposal Sys., Inc.*, 465 U.S. 822, 830 n.7 (1984); see also *Mississippi Power & Light Co.* v. *Mississippi*, 487 U.S. 354, 380-382 (1988) (Scalia, J., concurring in the judgment); *Dole* v. *United Steelworkers*, 494 U.S. 26, 54-55 (1990) (White, J., dissenting).

under Section 201, the Commission was not required to regulate that transmission component under Section 206.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

BARBARA D. UNDERWOOD
Acting Solicitor General

EDWIN S. KNEEDLER
Deputy Solicitor General

AUSTIN C. SCHLICK
Assistant to the Solicitor General

KEVIN P. MADDEN
General Counsel

CYNTHIA A. MARLETTE
Deputy General Counsel

SUSAN J. COURT
Associate Solicitor

TIMM L. ABENDROTH
DAVID H. COFFMAN
Attorneys
Federal Energy Regulatory Commission

MAY 2001

(18) (17)

Nos. 00-568 & 00-809

JUN 2 2001

IN THE

Supreme Court of the United States

Supreme Court, U.S.
FILED
JUL 2 2001
OFFICE OF THE CLERK

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

---

REPLY BRIEF OF ENRON POWER MARKETING, INC. AS PETITIONER IN NO. 00-809

JEFFREY D. WATKISS
BRACEWELL & PATTERSON, L.L.P.
2000 K Street, N.W.
Suite 500
Washington, D.C. 20006
(202) 828-5800

JOSEPH R. HARTSOE
SARAH NOVOSEL
ENRON CORPORATION
1775 I Street, N.W.
Washington, D.C. 20006
(202) 828-3360

LOUIS R. COHEN
Counsel of Record
JOSEPH E. KILLORY, JR.
JONATHAN J. FRANKEL
IJAY PALANSKY
MICHAEL PLOTNICK
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000

Counsel for Petitioner Enron Power Marketing, Inc.

---

20 pp

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

INTRODUCTION AND SUMMARY 1

ARGUMENT 5

I. THE FEDERAL POWER ACT GRANTS FERC JURISDICTION OVER ALL TRANSMISSION OF ELECTRIC ENERGY IN INTERSTATE COMMERCE, INCLUDING TRANSMISSIONS WHOSE COST IS BUNDLED INTO A RETAIL SALES CHARGE. 5

A. The FPA Is Not Ambiguous with Respect to FERC's Jurisdiction over Interstate Transmission. 5

B. Application of the OATT to Interstate Transmissions Bundled with Retail Sales Is Consistent with the Federal/State Regulatory Scheme of the FPA and Does Not Interfere with Traditional State Regulation. 10

II. TRANSMISSION-OWNING UTILITIES CAN AND DO DISCRIMINATE AGAINST COMPETING USERS OF TRANSMISSION SERVICE, AND FERC'S FAILURE TO ADDRESS THIS DISCRIMINATION WAS UNLAWFUL. 12

A. EEI's Argument that There Can Be No Undue Discrimination with Respect to Transmissions Bundled with Retail Sales Is Wrong as a Matter of Both Law and Fact. 13

B. FERC's Arguments that Coverage of Transmission for Bundled Service Is Not "Necessary" Are Also Unavailing. 15

CONCLUSION 20

TABLE OF AUTHORITIES

CASES

Page(s)

Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission, 461 U.S. 375 (1983) 18

Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) 1, 5

FPC v. Conway Corp., 426 U.S. 271 (1976) 11

FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) ..... *passim*

FPC v. Southern California Edison Co., 376 U.S. 205 (1964) 9

Maryland People's Counsel v. FERC, 761 F.2d 768 (D.C. Cir. 1985) 9

Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953 (1986) 6

Northern States Power Co. v. FERC, 176 F.3d 1090 (8th Cir. 1999), *cert. denied*, 528 U.S. 1182 (2000) 4, 20

Public Utilities Commission of Rhode Island v. Attleboro Steam & Elec. Co., 273 U.S. 83 (1927) 11

Ratzlaf v. United States, 510 U.S. 135 (1994) 7

SEC v. Chenery Corp., 332 U.S. 194 (1947) 15

United Distribution Cos. v. FERC, 88 F.3d 1105 (D.C. Cir. 1996) 10

United States v. Public Utilities Commission of California, 345 U.S. 295 (1953) 9

STATUTES

Natural Gas Act, 15 U.S.C. § 717 *et seq.*

15 U.S.C. § 717(b) 9

15 U.S.C. § 717f(c) 9

Federal Power Act, 16 U.S.C. §§ 792 *et seq.*

16 U.S.C. § 824(b) ..... *passim*

16 U.S.C. § 824e(a) 1

TABLE OF AUTHORITIES — Continued

Page(s)

16 U.S.C. § 824e(d) 11

16 U.S.C. § 824k(h) 12

ADMINISTRATIVE CASES & MATERIALS

American Electric Power Service Corp., 64 F.E.R.C. ¶ 61,279 (1993) 4, 14

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Wellhead Decontrol, Order No. 636, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 30,939, 57 Fed. Reg. 13,267 (1992) 9

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation Under Part 284 of the Commission's Regulations, Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol and Order Denying Rehearing in Part, Granting Rehearing in Part, and Clarifying Order No. 636, Order No. 636-A, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 30,950, 57 Fed. Reg. 36,128 (1992) 10

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Transmitting Utilities, Order No. 888, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996) .... *passim*

TABLE OF AUTHORITIES — Continued

Page(s)

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-A, [Reg. Preambles] III F.E.R.C. Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274 (1997) 1, 12, 16, 17

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats. & Regs. ¶ 32,514, 60 Fed. Reg. 17,622 (1995) 1

Regional Transmission Organizations, Order No. 2000, [Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,089, 65 Fed. Reg. 809 (2000) 19

OTHER AUTHORITIES

Comments of the Transmission Access Policy Study Group On Major Policy Issues, Nos. RM95-8-000 et al. (FERC filed Aug. 7, 1995) 17

Comments of the Transmission Access Policy Study Group on Basic Assumptions, Nos. RM95-8-000 et al. (FERC filed May 24, 1996) 17

Initial Comments of The Coalition for a Competitive Electric Market, Nos. RM95-8-000 et al. (FERC filed July 12, 1995) 17

Request for Clarification and Rehearing of the Transmission Access Policy Study Group and Certain of Its Members, Nos. RM95-8-000 et al. (FERC filed May 24, 1996) 17

INTRODUCTION AND SUMMARY

In Orders No. 888 and 888-A, FERC found that the public utilities that own interstate transmission facilities discriminate, with respect to terms of access and usage, against other suppliers of electricity and in favor of their own transmissions. *See, e.g.*, NOPR at 33,052, Pet App. 566a; Order No. 888 at 31,682, 31,919-26, Pet. App. 214a, 315a-331a; Order No. 888-A at 30,210, Pet. App. 435a; (FERC Br. at 11). Pursuant to its statutory mandate to eliminate undue discrimination, 16 U.S.C. § 824e(a), FERC ordered such utilities to end discrimination between (a) the transmission they provide to competing suppliers and (b) the transmission they provide to themselves for their own (i) wholesale sales and (ii) *un*bundled retail sales. But although FERC concluded that it would be "helpful" also to require such utilities to take transmission service for their *bundled* retail sales on the same nondiscriminatory terms, Order No. 888 at 31,699, Pet. App. 235a, it read the Federal Power Act (FPA) as denying it jurisdiction to do so. It therefore allowed the utilities to continue to discriminate in favor of their own transmissions that account for about 60% of the pertinent usage of the interstate grids. (*See* Enron Pet. Br. at 5.)

The D.C. Circuit upheld FERC's abdication of jurisdiction over transmissions to serve bundled retail sales on the ground that the FPA is ambiguous and therefore the agency is entitled to deference under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). In this Court, FERC urges affirmance primarily on that ground. Respondents New York et al. (New York) and Edison Electric Institute (EEI), the trade association of transmission-owning utilities, argue in addition that FERC jurisdiction over such transmissions would interfere with the traditional authority of the states over retail sales. EEI argues further that in any event there is no discrimination because, it alleges, there is no competition to serve bundled retail customers. All of these arguments are wrong.

Preliminarily, four important points are not open to serious dispute. First, "transmission" of electric energy at high voltage over a grid is distinct, as both a physical matter and a statutory matter, from "distribution" at low voltage over radial electric lines. (*See* Enron Resp. Br. in No. 00-568, at 28-32; FERC Br. at 30-34; Transmission Access Policy Study Group (TAPS) Br. at 21-24; Electrical Engineers et al. (Experts) Br. at 26.) Second, transmission is exactly the same, and uses the grid in the same way, regardless of whether the transmitted energy is sold on a bundled or unbundled basis. (*See* Enron Pet. Br. at 4-5, 30-31; Experts Br. at 2, 8-11, 14-17.) Third, section 201 of the FPA, 16 U.S.C. § 824(b), gives FERC "jurisdiction over public utilities' transmission of energy in interstate commerce 'without qualification.'" (FERC Br. at 13; *see also* Enron Pet. Br. at 21-27.) Fourth, except for some transmissions within Texas, virtually all electric transmission within the contiguous United States is "in interstate commerce" because (a) every transmission over an electric grid uses the entire grid (*see* FERC Br. at 27; TAPS Br. at 27-30; Experts Br. at 2-3, 10-11, 16-17), and (b) today (although this was not true in 1935) all non-Texas transmission lines are interconnected. (*See* Enron Pet. Br. at 9, 28; FERC Br. at 4-5, 25-27; Experts Br. at 2-3, 19, 30.)

FERC's argument that there is an "ambiguity" with respect to FERC's jurisdiction is not based on the language of section 201(b)(1) regarding transmission. FERC concedes that this provision would, standing alone, grant jurisdiction over all transmission in interstate commerce. (*See* FERC Br. at 28-29, 45.) FERC contends that ambiguity is created by the Act's separate confirmation of state jurisdiction over retail *sales* of electric energy. New York and EEI go further, arguing that FERC jurisdiction over interstate transmission, if construed to reach transmissions that serve bundled retail sales, would interfere with authority Congress left to the states.

There is no ambiguity and no interference, as this Court has already held in interpreting the parallel provisions of the

Natural Gas Act. *See FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 637-38 (1972) (*LP&L*). Interstate transmission, like interstate transportation of natural gas, is *both* a federally regulated activity *and* a component of bundled retail service whose cost is factored into state-regulated retail rates. Federal regulation of such transmission is perfectly compatible with plenary state regulation of retail sales, just like federal regulation of railroad charges for carrying coal to a utility's generators or federal regulation of the communications charges the utility incurs in doing business. The rights of the states to decide who may serve their retail customers and to dictate the terms and quality of that service are not challenged by anyone and not at issue.

This case is not, however, solely or primarily about the price charged for transmission: it is about fair and nondiscriminatory access to and usage of the interstate grids,[1] based on a published tariff that sets forth rules of access, procedures for scheduling and information sharing, rules for curtailment in periods of system constraint, and similar matters. (*See* TAPS Br. at 31-38 (describing the "inherent[ ] unworkab[ility]" of state regulation, and necessity for federal regulation, of the interstate grids).) Respondents argue that because bundled retail customers normally have no choice of supplier, there is no competition, hence no discrimination,

---

[1] As amicus Pennsylvania Public Utility Commission points out (Br. at 7):

> New York[ ] . . . erroneously conflates State ratemaking powers with rules controlling the operation of the interstate transmission network. Transmission rates are actually a relatively small component of retail electric rates. It is clear from New York's argument (and even more so from the novel theory advanced by California . . .) that retail rates are not the issue here. Network control and 'rules of the road' are what is being fought over. Who controls the interstate grid gets to decide a great many things, including wholesale generation market design and which wholesale electricity transactions will flow and which will be cut or reduced.

and hence no need for any regulation of interstate transmission other than whatever review of transmission costs a state chooses to conduct in connection with retail ratemaking. But all transmission competes for access to the interstate grids, whether the ultimate retail sale is unbundled or bundled and, as FERC has recognized, a transmission owner unduly discriminates when it treats other transmission users less favorably than it treats itself, whether or not they are competing for the same energy customer. *See American Elec. Power Serv. Corp.*, 64 F.E.R.C. ¶ 61,279 (1993). Moreover, utilities that serve bundled retail customers do compete with other suppliers for various important classes of customers (e.g., municipalities, cooperatives, large industrial customers) and their ability to provide themselves with superior transmission stifles that competition.

FERC's decision to abdicate its jurisdiction over transmissions whose cost is bundled with retail sales of energy leaves a regulatory vacuum that all but invites interstate conflict. Users in every contiguous state depend on the interstate transmission grids, including the portions that lie in other states, to receive electricity from close and distant generators. Current events vividly demonstrate that capacity on those grids is often short. The open access regime was intended as a uniform set of rules for allocating that capacity fairly. But as some states (*see* PA Br. at 3-4, 15) have recognized, FERC, by disclaiming jurisdiction, has permitted a state to circumvent true open access, and beggar its neighbors, by asserting a superior claim to the in-state portion of the interstate grid capacity for *its* bundled retail customers, making that capacity unavailable for other states' through transmissions. One court of appeals has explicitly allowed this to happen. *See Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999), *cert. denied*, 528 U.S. 1182 (2000). No state can protect itself from its neighbors' selfish use of "their" parts of the grid, because no state has jurisdiction to regulate the out-of-state portions of interstate lines. FERC's

abdication threatens the nationwide markets for power that Congress sought to build.

ARGUMENT

I. THE FEDERAL POWER ACT GRANTS FERC JURISDICTION OVER ALL TRANSMISSION OF ELECTRIC ENERGY IN INTERSTATE COMMERCE, INCLUDING TRANSMISSIONS WHOSE COST IS BUNDLED INTO A RETAIL SALES CHARGE.

A. The FPA Is Not Ambiguous with Respect to FERC's Jurisdiction over Interstate Transmission.

The D.C. Circuit ruled, and FERC argues in this Court, that the FPA is ambiguous and that FERC's determination that it lacked jurisdiction over transmissions bundled with retail sales is therefore entitled to deference. But the relevant provision of the FPA is not ambiguous, and the agency and courts are bound by what it plainly says. *See Chevron*, 467 U.S. at 842-43.

Section 201(b) gives FERC jurisdiction over "the transmission of electric energy in interstate commerce . . . ." 16 U.S.C. § 824(b). As FERC recognizes (*see* Br. at 45), there is no stated qualification or limitation based on the terms of the ensuing sale or on anything else. *Cf. LP&L*, 406 U.S. at 637-38 (finding no limitation in the parallel NGA provision). Instead, FERC argues that an ambiguity is created, leaving room for FERC interpretation, because "[s]ection 201(b) also assigns the states jurisdiction over 'any . . . sale of electric energy' that is not 'at wholesale in interstate commerce.'" (Br. at 45.)

But there is no conflict between the two parts of section 201(b), and there is no ambiguity for FERC to resolve. The terms of transmission in interstate commerce, including all aspects of access to and usage of the interstate grids, are explicitly subject to FERC jurisdiction. The cost of transmis-

sion is one of a number of component costs incurred by a retail utility that are clearly subject to federal regulation (including the cost of power purchased at wholesale). Such federal regulation does not usurp any state regulatory power, including the states' right to regulate the retail price of electricity. It simply means that if a state regulator chooses to use cost-based rate-setting, then it must take a utility's federally determined costs into account in setting a final price. *Cf. Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 966 (1986).

EEI asserts that, in the case of bundled retail sales, interstate transmission becomes an "inseparable" part of the retail "sale of electric energy." (Br. at 38.) But transmission and the sale of energy are no more "inseparable" (in the sense of being impossible to regulate separately) than the (federally regulated) cost of transporting a good to market and the (state regulated) act of selling it. Bundling does not turn the transmission into a sale, and transmission uses the grids the same way, regardless of how its cost is reflected on the end user's power bill. The very word "bundling" implies that different things—here generation, transmission, and delivery—are wrapped together for purposes of sale.[2]

EEI adds (*see id.* at 38) that since section 201(b) unambiguously gives FERC jurisdiction over wholesale sales in interstate commerce, the additional language confirming state jurisdiction over "any other sale of electric energy" must be interpreted to mean "the *transmission* of energy for retail sale," because otherwise the "any other sale" language would be superfluous. As it happens, this Court has already rejected

---

[2] EEI contradicts its own argument by conceding that, even when transmission is bundled with the retail sale of energy, FERC retains jurisdiction to review the utility's "'set aside' for bundled retail service (i.e., for 'native load'), to ensure that utilities do not arbitrarily withhold transmission capacity from the open access market." (Br. at 48; *see also* NY Br. at 18 (conceding that FERC has jurisdiction to "limit[ ] the ability of a utility to reserve transmission capacity for native load to levels needed to accommodate reasonable growth") (citations omitted).)

this remarkable argument. Interpreting the parallel language in the NGA, the Court determined that Congress was simply adding belt to suspenders:

> It is well established that the proviso [to section 1(b) of the Natural Gas Act, denying the FPC jurisdiction over "any other . . . sale of natural gas"] was added to the Act merely for clarification and was not intended to deprive FPC of any jurisdiction otherwise granted by § 1(b). The House report on the bill described this second sentence of § 1(b) as follows: "The quoted words are not actually necessary, as the matters specified therein could not be said fairly to be covered by the language affirmatively stating the jurisdiction of the Commission, but similar language was in previous bills, and, rather than invite the contention, however unfounded, that the elimination of the negative language would broaden the scope of the act, the committee has included it in this bill."

LP&L, 406 U.S. at 637-38 n.14 (quoting H.R. Rep. No. 75-709, at 3 (1937)).

FERC argues (*see* Br. at 46) that the "legislative history of the FPA is inconclusive," but legislative history—in particular "inconclusive" legislative history—cannot make a clear statute ambiguous. *See Ratzlaf v. United States*, 510 U.S. 135, 147-48 (1994). Moreover, the legislative history that FERC, New York, and EEI cite does not suggest any ambiguity. All three respondents point to language preserving "the authority of States to fix local rates." (FERC Br. at 46; NY Br. at 8; EEI Br. at 39 n.30.) But this state authority does not obscure FERC's authority to regulate interstate transmission any more than it obscures FERC's authority to regulate wholesale sales. As Enron showed in its opening brief (Br. at 23-25), the legislative history of the FPA in fact supports FERC jurisdiction over all interstate transmission, wholesale or retail, bundled or unbundled. FERC's and New York's unsuccessful attempts to answer this showing (*see*

FERC Br. at 46; NY Br. at 7-12) misread statements in the legislative history about retail sales as if they were discussing transmission and, in the case of New York, confuse transmission with distribution (*see* NY Br. at 11).

Finally, contrary to respondents' arguments, this Court's decision in *LP&L* is directly on point. At issue in *LP&L* was FERC's jurisdiction to include bundled retail sales of natural gas in FPC-ordered curtailment plans during periods of short supply. The Court held that section 1(b) of the Natural Gas Act (NGA), 15 U.S.C. § 717(b), which parallels and is nearly identical to section 201(b) of the FPA, granted FERC jurisdiction over the transportation of natural gas, even when transportation was bundled with a retail sale. 406 U.S. at 636-37.

FERC acknowledges that *LP&L* "confirms that the Commission's jurisdiction over interstate transmission is in addition to, and is not limited by, its jurisdiction over wholesale sales." (Br. at 19-20; *see also id.* at 28-29.) But FERC later, inconsistently, describes the pertinent holding of *LP&L* as limited to "federal curtailment requirements." (*Id.* at 46-47.) The latter description is wrong: *LP&L* suggests no such limitation and, perhaps more important, curtailment rules—a key feature of rules ensuring equal access to the grids—are close to the heart of this case. *See infra* pp. 19-20.

FERC argues further that *LP&L* is distinguishable on the grounds that (a) the federal curtailment requirements in *LP&L* addressed transportation and did not affect retail rate-setting, and (b) regulation of interstate transportation in *LP&L* was necessary to prevent conflicts among the states. (*See* FERC Br. at 37.) But similar conditions obtain here: the OATT addresses interstate transmission, not retail rate-making, and its indirect effect on retail rates is not qualitatively different from the potential indirect effect of the regulations at issue in *LP&L*. And, as further discussed at pp. 17-19, *infra*, the absence of federal regulation of important inter-

state transmission will create jurisdictional gaps and make state conflicts almost inevitable.

EEI's attempts to explain away *LP&L* also fail. EEI's first answer to *LP&L* is that the Court's practice of citing the FPA and NGA interchangeably does not apply to the jurisdictional provisions. (*See* EEI Br. at 42.) EEI is simply wrong. In *FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964), for example, the Court held that its review of the FPA's jurisdictional grants in section 201(b) did not proceed "on a clean slate. . . . The Natural Gas Act grew out of the same judicial history as did the part of the [FPA] with which we are here concerned; and § 201(b) of the Power Act has its counterpart in § 1(b) of the Gas Act . . . ."). *Id.* at 211-12.[3]

EEI also argues that *LP&L* is distinguishable because, EEI asserts, it dealt with section 7(c) of the NGA, a provision with no FPA parallel, which requires natural gas companies to obtain FPC certificates of public convenience before transporting natural gas, 15 U.S.C. § 717f(c). But this Court's confirmation of FPC jurisdiction over all natural gas transportation did not rest on section 7(c), and there is no indication that the Court believed that section 7(c) augmented that jurisdiction. The Court expressly rejected the lower court's holding that FERC must have been acting under its section 7 authority because it lacked jurisdiction under section 1(b), holding instead that the FPC acted under its authority in sections 1(b) and 4. *See LP&L*, 406 U.S. at 643-46.[4]

---

[3] *See also United States v. Public Utilities Comm'n of California*, 345 U.S. 295, 310-11 (1953) (noting that NGA precedent "would be as applicable here [interpreting FPA § 201(b)] as to § 1(b) of the [NGA]").

[4] EEI also argues that the NGA precedent is inapposite because the natural gas industry was not characterized by vertically integrated entities, as the electric industry is. But EEI greatly exaggerates. Before the complete unbundling of the gas industry pursuant to FERC Order No. 636, 57 Fed. Reg. 13,267 (Apr. 16, 1992), there had always been significant vertical integration of gas pipelines with both gas production and distribution. *See, e.g., Maryland People's Counsel v. FERC*, 761 F.2d 768, 775 (D.C. Cir. 1985) ("Most, if not all, major gas pipelines . . . are

B. Application of the OATT to Interstate Transmissions Bundled with Retail Sales Is Consistent with the Federal/State Regulatory Scheme of the FPA and Does Not Interfere with Traditional State Regulation.

The general problem addressed in Orders No. 888 and 888-A is relatively new. In the era when vertically integrated utilities, mostly confined to single states, served almost all retail customers on a state-regulated monopoly basis, the problem of competitive access to and usage of the interstate grids was presented only in unusual situations. *See* Order No. 888 at 31,639-47, Pet. App. 140a-161a; (TAPS Br. at 4, 38-41.) The need for general open, nondiscriminatory access arose in the early 1990s, when new federal legislation led to widespread interstate competition to supply electric energy and the new suppliers, lacking transmission facilities, needed access to the facilities owned by the traditional utilities in order to bring electricity into the states where it was needed. *See* Order No. 888 at 31,639-47, 31,651-52, Pet. App. 140a-161a, 170a-172a; (Enron Pet. Br. at 9-11; FERC Br. at 9-12).

This newly acknowledged problem was one that the states had not previously regulated. Traditional state regulation of bundled retail sales did not purport to regulate the

'backward vertically integrated'—that is, they own significant gas exploration, development and production affiliates.") (citations omitted). And just as in the electric industry, FERC found that the gas pipelines had an incentive to, and did, discriminate in favor of their own and affiliated gas production. *See Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Wellhead Decontrol*, Order No. 636-A, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 30,950, at 30,542 (1992) ("major purpose of the Commission in adopting Order No. 636 is to design rules to counter th[e] economic incentive to discriminate in favor of a pipeline's own bundled sales service") (citation omitted), *aff'd in relevant part sub nom. United Distribution Cos. v. FERC*, 88 F.3d 1105, 1125 (D.C. Cir. 1996) (upholding mandatory unbundling to prevent pipelines from providing superior transportation to their own bundled gas sales).

transmission of electric energy across state lines. What EEI describes (Br. at 36) as "five or more decades" of "state commissions . . . asserting jurisdiction over the transmission aspect of such sales" has consisted of state authorities taking transmission costs into account when determining retail rates and imposing service level requirements for their own local customers. (*See* FERC Br. at 46-47.) Application of the OATT to transmissions of energy for bundled retail sale would not displace state regulation: the states would simply continue to take transmission costs (although now subject to the OATT) into account when determining retail rates.[5]

But, more important, the OATT is not primarily about rates at all: it is about setting uniform rules for access to and usage of the interstate grids. As such, the OATT is qualitatively unlike anything any state has ever done or could ever do; it is simply inconceivable that open access could be achieved other than by a federal agency imposing compatible terms on all owners of the facilities that together make up the grids. (*See* TAPS Br. at 31-38.)[6] State commissions have no authority or incentive to impose nondiscriminatory conditions for competitive access to the interstate grids by out of state suppliers servicing out of state users, *see, e.g.*, *Public*

5 Contrary to New York's argument (Br. at 6), FPA section 206(d), 16 U.S.C. § 824e(d), which gives FERC authority to investigate and "determine" the cost of interstate transmission "in cases where [FERC] has no authority to establish a rate governing the sale of [the] energy," supports Enron's position: it provides that, even where there is a bundled retail sale, FERC may, on its own motion, decide the costs of interstate transmission.

6 EEI argues (Br. at 41) that applying the OATT to transmissions bundled with retail sales would impose "a huge regulatory burden and uncertainty on the industry." But as FERC notes (Br. at 43 (citing *FPC v. Conway Corp.*, 426 U.S. 271, 280 & nn.6, 7 (1976)), "the resulting accounting issues would be commonplace." Utilities providing bundled service regularly need to account separately for federally regulated and state-regulated costs. And of course the fact that electric service is unbundled in many states (*see* EEI Br. at 11 n.6) means that the OATT is already broadly applicable to utilities that sell at retail in such states.

Utilities Comm'n of Rhode Island v. Attleboro Steam & Elec. Co., 273 U.S. 83 (1927); *LP&L*, 406 U.S. at 633-36 (noting that conflicting interests among states preclude workable state regulation of interstate natural gas transportation).

Finally, New York and EEI argue (*see* NY Br. at 7, 16; EEI Br. at 40-41) that Enron is attempting to compel FERC to violate FPA section 212(h), 16 U.S.C. § 824k(h), which bars FERC from "requir[ing] the transmission of electric energy . . . directly to an ultimate consumer." But Enron is arguing only that FERC has jurisdiction over transmission in which a utility in fact engages, and that FERC must use that authority to eliminate undue discrimination between users of interstate transmission facilities. Neither FERC nor Enron contemplates giving FERC authority to order direct transmission to an ultimate consumer. *See, e.g.*, Order No. 888 at 31,781, Pet. App. 306a-307a. The significance of section 212(h) for this case is that its express limitation, barring FERC from ordering transmission to retail customers, would be meaningless if, as New York contends, FERC's jurisdiction over interstate transmission extended only to transmissions supporting wholesales.

II. TRANSMISSION-OWNING UTILITIES CAN AND DO DISCRIMINATE AGAINST COMPETING USERS OF TRANSMISSION SERVICE, AND FERC'S FAILURE TO ADDRESS THIS DISCRIMINATION WAS UNLAWFUL.

In the orders under review, FERC found that the "vast majority" of vertically integrated utilities "historically have declined to transport electric energy that would compete with their own sales or have offered access that is inferior to what they use for their own sales," Order No. 888-A at 30,210, Pet. App. 436a-437a, and that "[t]he *only* way . . . to remedy [such] discrimination is through readily available, nondiscriminatory transmission access," *id.* at 30,176, Pet. App. 382a (emphasis added). These findings made no distinction between transmissions for bundled and unbundled retail

sales; on the contrary, the orders find that "all" transmission must be subject to open access if consumers are to realize the benefits of supply competition. *See* Order No. 888 at 31,635, Pet. App. 133a. But even though FERC acknowledged it has a "statutory obligation under sections 205 and 206 of the Federal Power Act" to remedy undue discrimination, *id.*, it simply shrugged that task off with respect to the majority of transmissions on the interstate grids: without explanation or citation to the record, FERC declared that it was "not . . . necessary" to apply the OATT to transmissions where the ensuing sale is bundled retail. *Id.* at 31,699, Pet. App. 235a. The result is a serious regulatory gap.

A. EEI's Argument that There Can Be No Undue Discrimination with Respect to Transmissions Bundled with Retail Sales Is Wrong as a Matter of Both Law and Fact.

EEI suggests (Br. at 46-47) that there can be no "undue discrimination" within the meaning of sections 205 and 206 because (it asserts) alternative suppliers do not compete with vertically integrated utilities for their bundled-service retail customers, and the unbundled-service customers for whom the new entrants compete are not "similarly situated" to the transmission monopolists' bundled native load. This is wrong on both the law and the facts.

First, although EEI attributes to FERC the suggestion that "undue discrimination" can exist only as between similarly situated retail customers (*see id.* at 47), the agency has specifically rejected that narrow conception of discrimination. As FERC noted in Order No. 888, the development of competition after the EPAct required the agency to "broaden[] its undue discrimination analysis (which traditionally had focused on the rates, terms, and conditions faced by similarly situated third-party customers) to include a focus on the rates, terms, and conditions of a utility's own uses of the transmission system." Pet. App. 160a-161a. Transmission monopolists and other suppliers do compete head-to-

head for capacity on the interstate grids, even when they are using that capacity to serve different classes of customers, or customers in different states. For that reason, FERC held, an "open access tariff that is not unduly discriminatory or anti-competitive should offer third parties access on the same or comparable basis, and under the same or comparable terms and conditions, as the transmission provider's uses of its system." Pet. App. 161a (quoting *American Elec. Power Serv. Corp.*, 67 F.E.R.C. ¶ 61,317, at 61,490 (1994)).

Second, EEI's factual premise—that vertically integrated utilities and other suppliers do not compete for the same customers—is incorrect. Even in a "bundled" state, suppliers compete to serve categories of large customers that have a choice to be part of the franchised utility's native load or use an alternative power source. These customers include municipalities,[7] and large industrial users that can build their own on-premises generators or exercise "buy through" rights permitting them, as part of an economic development package, to by-pass their local distribution monopoly and access competitive power suppliers. Such customers remain dependent on the franchised utility's transmission for delivery or back-up service, and the franchised utility can deter the customer from leaving by threatening to favor its own customers and withhold transmission or curtail access for others in times of constrained capacity. *See, e.g.*, Order No. 888 at 31,921, Pet. App. 320a (noting instances where vertically integrated utilities punished "prodigal [*sic*] customers" by withholding needed transmission).

Moreover, other suppliers compete directly with transmission monopolists for the same *wholesale* customers in "bundled" states, and FERC's failure to extend open access to bundled retail load impedes that competition. For example, Enron often competes with a vertically integrated utility

---

[7] *See, e.g.*, Order No. 888 at 31,920, 31,923-25, Pet. App. 316a-319a, 324a-330a (examples involving AMP-Ohio and various California municipalities).

to sell electricity to other, neighboring utilities, and to do so Enron's only, or most economical, transmission may be through the first utility's bundled-service territory. The exemption from open access for transmissions to serve bundled customers gives that utility an effective chokehold over Enron's "through" transmission: Specifically, that utility can tie-up for native load some or all of its incoming transmission capacity, thereby denying Enron "through" service or forcing Enron to schedule around the utility's bundled service territory. Order No. 888 cites several examples of strategic tying-up of transmission capacity, nominally for bundled transmissions, in order to block access by competing sellers. *See, e.g.*, *id.* at 31,920, 31,923-24, Pet. App. 317a-318a, 325a-328a (examples of utilities manipulating reservation of transmission capacity to discourage competition).

EEI's suggestion (*see* Br. at 47-48) that the exemption from open access for bundled transmission can somehow be justified as a protection for residential customers that cannot choose their suppliers inadvertently proves Enron's point. A state might *want* to give its own residents transmission priority over wholesale purchasers, but it does not and should not have jurisdiction to do so. On the contrary, the disadvantaged wholesale customers often are other utilities or municipalities with their own residential customers to serve; denying them equal access simply shifts the burden from residential users in one state to residential users in another.[8]

B. FERC's Arguments that Coverage of Transmission for Bundled Service Is Not "Necessary" Are Also Unavailing.

FERC suggests (Br. at 47) that its failure to extend open access to bundled transmission was actually a reasoned determination based on the state of the factual record then be-

---

[8] EEI's justification for distinguishing bundled from unbundled transmission service is not one that FERC ever invoked itself. *Cf. SEC v. Chenery Corp.*, 332 U.S. 194, 196 (1947).

fore it. The portions of the orders FERC cites demonstrate otherwise. The *entirety* of Order No. 888's analysis of the factual record on "necessity" reads as follows:

> Although the unbundling of retail transmission and generation, as well as wholesale transmission and generation, would be helpful in achieving comparability, we do not believe it is necessary.

Pet. App. 235a. FERC's other citation to its purported analysis of the factual record is simply the rehearing order's recitation of what the agency said the first time. *See* Pet App. 453a-454a. The claim that these passages represent a reasoned judgment that the factual record did not support an extension of open access is a considerable stretch.

In fact, as demonstrated above and in Enron's opening brief (*see* Pet. Br. at 12-13, 36-38), Order No. 888 contains detailed findings of pervasive undue discrimination by vertically integrated utilities providing bundled service to their native loads, and none of these findings suggests that the prevalence or impact of discrimination turns on how the transmission is invoiced to the retail customer.[9] On the contrary, Order No. 888 proclaims that extending open access to bundled transmission would be "helpful" in stopping the discrimination that FERC had found. Pet. App. 235a. FERC's Notice of Proposed Rulemaking recognized that limiting open access to unbundled transmission would "result in service under two separate arrangements—an explicit wholesale transmission tariff filed at the Commission and an implicit retail transmission tariff governed by a state regulatory body," presenting the risk that "the quality of transmission service for retail purposes will be superior to the quality of transmission service offered for wholesale purposes." Order No. 888-A at 33,081-82, Pet. App. 634a. FERC expressly "s[ought] comment on how this bifurcated approach would

[9] In fact, because there was little or no unbundling prior to Order No. 888, all of FERC's findings of undue discrimination occurred in bundled states.

affect the public utility's incentives to provide non-discriminatory open access wholesale transmission service," *id.* at 635a, and the comments Enron and other parties filed provided ample justification for extending open access to bundled transmission.[10]

FERC's suggestion (Br. at 47) that Enron has never established the need for a *federal* role with respect to bundled transmission, or demonstrated the practical limitations of state regulation, is wrong. Enron made such a showing throughout the administrative proceeding.[11] It is evident that where a transmission line crosses state boundaries, the states through which that line passes cannot each adopt a rule giving its own bundled in-state customers priority rights to use the line's capacity. As the Pennsylvania PUC emphasizes, "[a]n interstate transmission system riddled with 'holes' or 'blockades' created by the erection of local State rules seeking to protect 'native' bundled retail load would be injurious to interstate commerce, retail competition, regional reliability and at odds with Congressional intent." (Br. at 3; *see also id.* at 12-13.) Current events in the West are demonstrating that the competitive energy supply markets Congress created are

[10] Enron participated in the Order No. 888 rulemaking as a member of the Coalition for a Competitive Electric Market, which submitted comments advocating extension of the OATT to bundled retail transmissions. *See, e.g., Initial Comments of The Coalition for a Competitive Electric Market*, Nos. RM95-8-000 et al. (July 12, 1995) (*CCEM Initial Comments*) at 10 ("ineluctably discrimination will persist until there is a total unbundling and consumers of all transmission services, wholesale and retail, take service pursuant to a tariff at posted rates"); *id.* at 4-10; *see also Comments of the Transmission Access Policy Study Group On Major Policy Issues*, Nos. RM95-8-000 et al. (Aug. 7, 1995) at 12, 27-30; *Request for Clarification and Rehearing of the Transmission Access Policy Study Group and Certain of Its Members*, Nos. RM95-8-000 et al. (May 24, 1996) at 8-13.

[11] *CCEM Initial Comments* at 5-6, 13; *see also Comments of the Transmission Access Policy Study Group on Basic Assumptions*, Nos. RM95-8-000 et al. (May 24, 1996) at 2 ("a working infrastructure for a market must be established by [FERC]").

regional and national; they are also demonstrating that individual states face powerful pressures in times of shortage to hoard supply for in-state uses and to prevent the transfer of electricity across state lines. As this Court recognized well before any state had implemented retail unbundling, the "transmission of energy is an activity particularly likely to affect more than one State, and its effect on interstate commerce is often significant enough that uncontrolled regulation by the States can patently interfere with broader national interests." *Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983) (citations omitted). FERC is the only entity capable of adopting consistent regulations and safeguarding the national interest.[12]

FERC also (inadvertently) acknowledges, in its discussion of unbundled transmission, the inherent limitations on state power that create a regulatory gap applicable to bundled transmissions as well. FERC explains (Br. at 38) that if a retail customer's state has sole jurisdiction to regulate transmissions to serve that customer, then no authority, federal or state, can regulate transmission service through "intervening" states whose facilities are part of the grid that connect the generator and the customer:

> If the State in which the retail customer is located has jurisdiction to regulate all unbundled transmission associated with a retail sale, there would be a large regulatory gap when the retail customer purchases power from a supplier in a distant State, and that supplier requires transmission service from intervening out-of-state utilities to deliver the power. The intervening transmission would be beyond the jurisdictional reach of the consumer's State . . . [and] would not be subject to meaningful regulation.

FERC means to be answering New York's contention that the states, not FERC, have jurisdiction over transmission to serve unbundled retail customers, but the point applies equally to transmission that serves bundled retail customers: absent FERC jurisdiction there can be *no* effective regulation of such transmission insofar as it implicates facilities in states other than the state of the retail customer. And FERC cannot fully protect the choices of retail customers in unbundled states if it cannot fully regulate the portions of the interstate grid that lie in "intervening" bundled states. (*See* TAPS Br. at 31-38.)

FERC seeks to reassure the Court that it can, in fact, police discrimination with respect to bundled transmission. (*See* Br. at 48; *see also* EEI Br. at 48-49.) FERC points to a later order (Order No. 2000) authorizing the creation of independent "regional transmission organizations" that would operate each grid in place of the vertically integrated utilities (*see* Br. at 47-48 n.23). But the formation of such organizations is entirely voluntary, *see* FERC Order No. 2000, 65 Fed. Reg. 810, 831-35 (Jan. 6, 2000), and one would not expect that the current monopolists—whose "inherent" incentives, FERC found, "make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors," Order No. 888 at 31,682, Pet. App. 214a—would willingly give up their strategic control over the transmission grids. FERC also states that it "continues to believe" it has full authority to prevent transmission monopolists from providing bundled transmission in a manner that disadvantages unbundled services subject to its jurisdiction. But in one of

---

12 New York's lengthy recitation of state-law analogues to the antidiscrimination provisions of the FPA and case law thereunder (*see* NY Br. at 19-23) proves nothing; as New York describes these cases, none involves protection of an out-of-state electric supplier against discriminatory reservations of capacity for in-state customers of in-state utilities. New York does not explain how it could impose consistent usage rules for the out-of-state portions of multistate transmission lines. And even taking New York at its word that it stands ready to police discrimination against out-of-state grid users, there is no guarantee other states will do likewise. Just the opposite: California has filed a brief in this case defending its claimed power to discriminate in favor of in-state users when there is a shortage of transmission capacity. (*See* Cal. Br. at 29.)

the critical situations—the determination of whether a utility can favor its own bundled service when system conditions require curtailment of transmission—the Eighth Circuit, following FERC's own reasoning here, held otherwise. *See Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999) (*NSP*), *cert denied*, 528 U.S. 1182 (2000).[13] FERC's unlawful abdication of its jurisdiction prevents it from playing the role that its own findings show is necessary.

CONCLUSION

The decision of the court of appeals sustaining FERC's abdication of jurisdiction over interstate electric transmission for bundled retail sales should be reversed.

---

[13] For the same reason, EEI's suggestion that in a curtailment situation "customers under the Order No. 888 open access tariff must receive the same degree of firmness as the utility's native load" rings hollow: this was the very requirement of Order No. 888 that the Eighth Circuit overturned on the basis of FERC's erroneous conclusion that it lacks jurisdiction over bundled transmissions. *NSP*, 176 F.3d at 1096 (overturning Order No. 888 requirement that firm transmission service to third parties be just as firm as bundled transmission to native load). Nor does FERC's limited ability to investigate vertically integrated utilities' purported reservations of transmission capacity for native load in individual cases, many months after the damage to competitors is done in the marketplace (*see* EEI Br. at 48-49), substitute for a self-enforcing structural remedy like the OATT, assuming that the ability to investigate even survives *NSP*.

Respectfully submitted,

JEFFREY D. WATKISS
BRACEWELL & PATTERSON, L.L.P.
2000 K Street, N.W.
Suite 500
Washington, D.C. 20006
(202) 828-5800

JOSEPH R. HARTSOE
SARAH NOVOSEL
ENRON CORP.
1775 I Street, N.W.
Washington, D.C. 20006
(202) 828-3360

LOUIS R. COHEN
Counsel of Record
JOSEPH E. KILLORY, JR.
JONATHAN J. FRANKEL
IJAY PALANSKY
MICHAEL PLOTNICK
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6000

Counsel for Petitioner Enron Power Marketing, Inc.

July 2, 2001

(19)

Supreme Court, U.S.
FILED
JUL 2 2001
CLERK

No. 00-568

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK and THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

REPLY BRIEF OF RESPONDENT CITIZENS ACTION COALITION OF INDIANA, INC.

RECEIVED
JUL 9 2001
LLC

MICHAEL A. MULLETT
Counsel of Record
MULLETT & ASSOCIATES
309 West Washington Street
Suite 233
Indianapolis, Indiana 46204
(317) 636-5165

Attorney for Respondent Citizens Action Coalition of Indiana, Inc.

167926

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

21 pp

TABLE OF CONTENTS

	Page
Table of Cited Authorities	ii
INTRODUCTORY STATEMENT	1
ARGUMENT	3
I. Congress Knew The Key Points Concerning Transmission Network Design, Evolving Transmission Technology And Infrastructure, And The Increasingly Interstate Nature Of The Industry When It Chose To Preserve State Jurisdiction In 1935.	3
A. The Context of the 1935 Act.	3
B. Congress' Knowledge of Transmission Technology, Interconnected Grids, Interstate Transmission Networks, and the Changing Nature of Their Use. ...	5
1. Facilities	5
2. Transmission	8
C. Congress' Informed Decision to Preserve State Jurisdiction.	9
II. Congress Affirmed Its 1935 Choice To Preserve State Jurisdiction In The 1992 Amendments.	11
III. The FERC Decisions TAPS Cites Do Not Show That FERC Regulated "Unbundled Retail Transmission" Before Order 888. ...	13
CONCLUSION	16

TABLE OF CITED AUTHORITIES

Page

Cases:

Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) 11

Consolidated Edison Co. of New York, 15 F.E.R.C. ¶ 61,174 (1981) 13, 14, 15

Director v. Perini, 459 U.S. 297 (1983) 1

Federal Election Comm'n v. NRA Political Victory Fund, 513 U.S. 88 (1994) 15

Niagara Mohawk Power Corp., 34 F.E.R.C. ¶ 61,028 (1986) 14

Niagara Mohawk Power Corp., 82 F.E.R.C. ¶ 63,018 (1998) 14

Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) 9

Pacific Gas & Elec. Co., 15 F.E.R.C. ¶ 63,059 (1981), *modified*, 20 F.E.R.C. ¶ 61,190 (1982) 15

Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n of Indiana, 332 U.S. 507 (1947) 9

Power Authority of State of New York v. Niagara Mohawk Power Corp., 79 F.E.R.C. ¶ 61,159 (1997) 14

Cited Authorities

Page

Steel Co. v. Citizens for a Better Environment, 523 U.S. 83 (1998) 15

Statutes:

15 U.S.C. § 717f 9

16 U.S.C. § 824(b)(1) 9

16 U.S.C. § 824a(b) 9

16 U.S.C. § 824j 11

16 U.S.C. § 824j(a) 11

16 U.S.C. § 824k(a) 11, 12

16 U.S.C. § 824k(g) 11

16 U.S.C. § 824k(h) 12

Rule:

Sup. Ct. R. 12.6 1

Other Authorities:

Legislative History of the Energy Policy Act of 1992: Senate Comm. on Energy and Nat. Resources, S. Prt. 103-91 (1994) 13

Cited Authorities

Page

H.R. Conf. Rep. No. 102-1018 (1992), *reprinted in* 1992 U.S.C.C.A.N. 2472 12

H.R. Conf. Rep. No. 1903, 74th Cong., 1st Sess. (1935) 3

H.R. Rep. No. 1318, 74th Cong., 1st Sess. (1935) ("1935 House Report") 4, 9, 10

Public Util. Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce, 74th Cong., 1st Sess. (1935) ("*Senate Hearings*") 4, 5, 6, 7, 8, 10

Public Util. Holding Companies: Hearings on H.R. 5423 Before the House Comm. on Interstate and Foreign Commerce, 74th Cong., 1st Sess., Pt. 1 (1935) ("*House Hearings*") 4, 5, 6, 7, 8

S. Rep. No. 621, 74th Cong., 1st Sess. (1935) ("1935 Senate Report") 3, 7, 9, 10

Robert L. Stern, Eugene Gressman, Stephen M. Shapiro & Kenneth S. Geller, *Supreme Court Practice* (7th ed. 1993) 1

INTRODUCTORY STATEMENT

Citizens Action Coalition of Indiana, Inc. (Citizens Action), a not-for-profit membership organization, represents the interests of residential consumers in utility-related matters. Citizens Action petitioned for review of Orders 888 and 888A, supported the position of the petitioners State of New York, *et al.* (State Commissions) in the Court of Appeals, and separately argued that the respondent Federal Energy Regulatory Commission (FERC) exceeded its statutory jurisdiction by asserting regulatory authority over unbundled retail transmission.[1] Accordingly, under Sup. Ct. R. 12.6, Citizens Action is a respondent in this Court, and is a respondent that is permitted to file briefs supporting the petitioner State Commissions. Robert L. Stern, Eugene Gressman, Stephen M. Shapiro & Kenneth S. Geller, *Supreme Court Practice* 324-25 (7th ed. 1993); *see, e.g.*, *Director v. Perini*, 459 U.S. 297, 304 (1983).

Citizens Action did not file an opening brief on the merits. Citizens Action submits this reply brief to answer the Respondents' repeated suggestions that technological and other changes allegedly unforseen by Congress justify FERC's action asserting jurisdiction over retail transmission under the Federal Power Act.

Taken as a whole, the several briefs opposing the State Commissions create the impression that the 1935 Congress foresaw only dimly, if at all, the key components of today's electric industry. FERC itself (Br. 5, 16-17) conveys the

---

1. *See* Initial Brief of Petitioners Opposing Stranded Cost Recovery at 52-53 (D.C. Cir. No. 97-1715); Reply Brief of Petitioners Opposing Stranded Cost Recovery at 24-26, 27-28 (D.C. Cir. No. 97-1715).

idea with statements that "[t]he interconnected nature of transmission grids, and their use in interstate commerce, have increased dramatically since 1935"; that electric utilities "[a]t that time" were "largely self-sufficient . . . with their own . . . facilities," and "sold their generation, transmission, and distribution services as a single bundled service to wholesale and retail customers"; and that the federal agency is now confronted with the problem of "applying the [Federal Power Act] to a new paradigm . . . not specifically contemplated by Congress in 1935 . . . ." This conception, that the interstate transmission grid has evolved into a new and qualitatively different reality, is the premise for arguments that regulatory policy should also evolve in ways that Congress did not intend.[2] This conception is wrong.

Considered individually, some of the characterizations of the 1935 grid are more or less accurate. The overall impression conveyed, however, is not. The key components of the electric industry, and their direction of change, were known in 1935 and were before the Congress when it made the decision to preserve State jurisdiction to the full extent it then existed. There have not been subsequent technological or other changes that make the 1935 Congress' choices about federalism impossible to implement, or even difficult to evaluate as applied to contemporary circumstances. There have not been subsequent legislative changes that call the 1935 Congress' choices into question. To the contrary, the Congress in 1992 affirmed the legislative decisions of 1935 on the basic division between State and Federal regulatory jurisdiction. Nor has there been any FERC regulatory practice inconsistent with Congress' decision to preserve state

2. *See, e.g.*, FERC Br. 16-17, 20-21, 39-40; Enron Resp. Br. 9-10, 25 n.13, 36-37, 39-40; TAPS Br. 4-10, 41-45; Pennsylvania PUC *amicus* Br. 3-4.

authority over all aspects of retail electric service, until the order on review in this case. It is not for FERC now to countermand the considered judgments of Congress.

ARGUMENT

I. Congress Knew The Key Points Concerning Transmission Network Design, Evolving Transmission Technology And Infrastructure, And The Increasingly Interstate Nature Of The Industry When It Chose To Preserve State Jurisdiction In 1935.

A. The Context of the 1935 Act.

The basic framework and most of the statutory sections that constitute today's Federal Power Act were enacted in 1935. The enacting legislation, however, contained more than that and had three parts:

(1) The Public Utility Holding Company Act of 1935.

(2) Amendments to the Federal Water Power Act of 1920 (which dealt with hydroelectric facilities, and which became what is known as Part I of the Federal Power Act).

(3) The provisions known as Parts II and III of the Federal Power Act, Part II of which establishes the scope of the FERC jurisdiction at issue in this case.

See S. Rep. No. 621, 74th Cong., 1st Sess., at 1, 4, 17 (1935) ("1935 Senate Report"); *see generally*, H.R. Conf. Rep. No. 1903, 74th Cong., 1st Sess. (1935).

The combination of the Public Utility Holding Company Act and the Federal Power Act in a single piece of legislation was not fortuitous. The basic design and much of the infrastructure of the Nation's electric industry had been developed by several large holding companies. *See* H.R. Rep. No. 1318, 74th Cong., 1st Sess. at 3 (1935) ("1935 House Report"); *Public Util. Holding Co. Act of 1935: Hearings on S. 1725 Before the Senate Comm. on Interstate Commerce*, 74th Cong., 1st Sess., at 797 (1935) ("*Senate Hearings*"). These holding companies created extensive multi-state electric systems by acquiring, combining and jointly operating many local electric utilities. Because of their interstate nature, the holding companies had grown beyond effective regulatory control of the States and had engaged in a variety of abuses. *Senate Hearings* at 3, 5, 798; *Public Util. Holding Companies: Hearings on H.R. 5423 Before the House Comm. on Interstate and Foreign Commerce*, 74th Cong., 1st Sess., Pt. 1 at 90, 407-09 (1935) ("*House Hearings*"). At the same time, however, the large and interstate electric systems they created were (at least in many instances) technologically and economically efficient and superior to isolated local electric utilities. *See, e.g.*, *House Hearings* at 534-35.

FERC's predecessor the Federal Power Commission (FPC) itself prepared the Federal Power Act parts of both H.R. 5423 and S. 1725 as introduced, and these FPC-sponsored parts were presented to the congressional committees by FPC Commissioner Seavy and FPC Solicitor DeVane. *House Hearings* at 383-84, 400-01, 449-50; *Senate Hearings* at 223. The Public Utility Holding Company Act part of the legislation would abolish or diminish the multi-state holding companies. As proposed by the FPC, Federal Power Act Part II was designed, *inter alia*,

to preserve (and further promote) large interstate electric "systems" while replacing holding company control with federal agency control. *See, e.g.*, *Senate Hearings* at 238-39 (FPC Solicitor DeVane); *House Hearings* at 517, 563-64 (same).

In the end, Congress was unwilling to grant the FPC powers anywhere near as expansive as requested in its proposed legislation. Instead, Congress reserved to the States all of the authority they then enjoyed. Because of the scope of the FPC's proposal, however, extensive hearings were held which made the Congress fully aware of the increasingly interstate nature of the industry and of the technological and economic factors that underlay these developments. Two aspects of the FPC's proposal, discussed below, are particularly significant in demonstrating the important features of the electric industry in 1935, and what Congress understood and foresaw at that time.

B. Congress' Knowledge of Transmission Technology, Interconnected Grids, Interstate Transmission Networks, and the Changing Nature of Their Use.

1. Facilities

The FPC's proposed legislation would have given the federal agency regulatory authority over the certification, construction and abandonment of transmission and generation facilities, and also authority to order interconnection between existing facilities. These FPC proposals appeared as Sections 203 and 204 in the original Senate and House bills, *Senate Hearings* at 40; *House Hearings* at 32, and were also described in the FPC's section-

by-section analysis submitted to the congressional committees, *Senate Hearings* at 246 (§§ 203-204); *House Hearings* at 385 (same). If granted, these powers would have given the FPC control over the basic physical design and development of the Nation's electricity system. *See, e.g.*, *House Hearings* at 392-93 (FPC Commissioner Seavy); *id.* at 501 (FPC Solicitor DeVane); *Senate Hearings* at 249-50, 279 (same).

In considering these proposed FPC powers, the congressional committees heard extensive evidence concerning the interstate electric system and its expansive growth. Maps depicting the geographical areas covered by the large interstate holding companies were presented. *House Hearings* at 264-65 (Lester Ready).[3] As one example, the "pink area" of one map showed "the area of the properties . . . affiliated with the Electric Bond & Share Co., and the United Corporation properties. . . . The major areas covered are the southeastern section, the New York area, Pennsylvania, Ohio, West Virginia, Michigan and such areas." *Id.* at 265. Other maps were presented depicting (1) the geographic coverage of "all transmission lines of 60,000 volts and over and . . . all power plants of 15,000 kilowatts and over" throughout the United States, and (2) lower voltage transmission lines over particular multi-state areas. *Id.* at 269-70. The expert testimony explained how with few exceptions the transmission networks did not correspond with state boundaries and encompassed multi-state territorial areas. *Id.*; *see also, e.g.*, *Senate Hearings* at 243-44 (FPC Solicitor DeVane).

3. Mr. Ready was identified as the Chief Consultant for the National Power Survey, a year-long federal study commissioned by Executive Order No. 6251. *House Hearings* at 263; *see also Senate Hearings* at 240, 798.

Congress also heard about the rapid expansion of interstate transmission facilities, and the concomitant increases in the proportion of the Nation's electricity transmitted across state boundaries. *House Hearings* at 266 (Mr. Ready); *id.* at 420 (FPC Commissioner Seavy); *see also* 1935 Senate Report at 17. By 1933, over 17% of all electricity was being transmitted across state lines, and that proportion had increased by more than 50% in just four years. *House Hearings* at 266 (Mr. Ready): *see also id.* at 420 (Commissioner Seavy); 1935 Senate Report at 17; 1935 House Report at 7. In many areas, the proportion transmitted across state lines by 1933 was substantially larger. For example, Pennsylvania exported over 40% of its electric generation while importing 20% as much as was generated within the Commonwealth. *House Hearings* at 267 (Mr. Ready). "New Hampshire and Vermont exported 61.1 and 70.8 percent, respectively, of the power . . . produced in those states," whereas Delaware imported virtually all of its power. *Id.* at 268-69. This information was presented for all 48 States and by selected multi-state regions. *Id.* at 267-68; *see also Senate Hearings* at 241-43 (FPC Solicitor DeVane).

Congress also heard about the continuing advances in transmission technology, including increased voltages (by that time, up to 285 kv.). *House Hearings* at 271 (Mr. Ready). Congress was informed that "[t]he longest single transmission line for large transmission of power [was] about 270 to 300 miles in length," and that for smaller exchanges of power there were systems interconnected "for as many as six and seven hundred miles." *Id.* at 270. The limits on transmission distance were described as a function of variable economic factors, including cost of fuel, cost of money, amount of power, and location of the market. *Id.* at 270-72.

Congress also heard about the concept and functioning of a transmission grid established by interconnection, and the term "grid" was even used. *Senate Hearings* at 277-78 (memorandum submitted by FPC Solicitor DeVane). Congress was told that "[t]he largest saving arising from a grid is the reduction of excess generating capacity in the interconnected area." *Id.* at 278. It was given an illustration involving "an area extending from Keokuk and St. Louis to Detroit, including Chicago and Milwaukee . . . ." *Id. See also, e.g.*, *House Hearings* at 271 (Mr. Ready); *Senate Hearings* at 274 (Solicitor DeVane).

2. Transmission

Another key part of the FPC's proposed legislation was Section 202, which provided, *inter alia*, that:

> (a) It shall be the duty of every public utility to . . . transmit energy for any person upon reasonable request therefor . . . .

Senate Hearings at 40; *House Hearings* at 32. This would have made utility transmission systems "common carriers" available for use by others. *House Hearings* at 395-96 (FPC Commissioner Seavy). Concomitantly, the FPC would be empowered to order utilities to "transmit energy for . . . one or more other persons." *Id.* at 32 (§ 203(b)); *Senate Hearings* at 40 (same). To support this FPC proposal, Congress was told about the many transmission service arrangements already existing by 1935. *House Hearings* at 533-35, 537 (FPC Solicitor DeVane); *Senate Hearings* at 271-72 (Statement submitted by Solicitor DeVane).

C. Congress' Informed Decision to Preserve State Jurisdiction.

The 1935 Congress declined to enact these parts of the FPC's proposed legislation. The Senate eliminated the provisions that would have given the FPC authority over the certification, construction and abandonment of transmission and generation facilities. 1935 Senate Report at 20.[4] The Senate also eliminated the FPC's proposed "common carrier" provisions that would have required utilities to transmit electricity for other persons. *Id.* at 19; *see also Otter Tail Power Co. v. United States*, 410 U.S. 366, 374 (1973); *id.* at 384-86 (Stewart, J., concurring in part and dissenting in part).

Congress did give the FPC authority to order interconnection, although only upon the request of a utility or state commission (and subject to other limitations). 1935 Senate Report at 19; 1935 House Report at 8, 27-28; *see* 16 U.S.C. § 824a(b). The Congress did so knowing that the increased interconnection would further increase the

---

4. The House subsequently eliminated all general FPC jurisdiction over generation facilities. 1935 House Report at 27; *see* 16 U.S.C. § 824(b)(1). The Federal Power Act is quite different from the Natural Gas Act in this respect. Under the Natural Gas Act, the FPC (now FERC) is given regulatory authority over the certification, construction and abandonment of gas transmission facilities (including a federal eminent domain power), 15 U.S.C. § 717f, and the interstate gas facilities subject to this FERC jurisdiction may be used for retail delivery, *see, e.g.*, *Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n of Indiana*, 332 U.S. 507, 509-10, 523 n.23 (1947). Congress has never given FERC any comparable regulatory authority over electric facilities, including transmission facilities, despite repeated proposals that it do so. *See, e.g.*, *Otter Tail Power Co. v. United States*, 410 U.S. 366, 386 & n.4 (1973) (Stewart, J., concurring in part and dissenting in part).

proportion of electricity transmitted across state lines. *See, e.g., Senate Hearings* at 241 (FPC Solicitor DeVane) ("Proper interconnection between these systems would tend to greatly increase the percentage [of power transferred across State lines]").

The 1935 Congress deleted and modified these provisions in the FPC's proposed bill at the request of state commissions. *See, e.g., Senate Hearings* at 749-50, 1083-84 (John Benton).[5] Congress decided instead to preserve and protect the regulatory jurisdiction of the States. 1935 Senate Report at 18; 1935 House Report at 8. The federal agency's jurisdiction was generally limited to areas where Congress believed the States could not legally or effectively regulate.[6]

When it made these fundamental political choices in 1935, Congress understood the key components of the electric industry, including interstate transmission systems, interconnected grids, continuing advances in transmission technology, the increasing proportions of power being transmitted across State boundaries, and the use of "common carrier" transmission service. These are still the key components of the industry today. As Justice Jackson noted

5. Mr. Benton was General Solicitor for the National Association of Railroad and Utilities Commissioners. *Senate Hearings* at 746.

6. The areas prominently mentioned were regulation of wholesale rates in interstate commerce; determination of costs of interstate facilities used for retail service (for purposes of ratemaking by State commissions); regulation of interstate consolidations and interconnections; and establishment of regional districts. 1935 Senate Report at 48, 51; 1935 House Report at 7-8.

for the Court, Congress made its fundamental choices in 1935 based not solely upon "engineering and scientific" facts concerning the interstate grid, but rather in significant part upon considerations of federalism and "the existence and vitality of these state governments." *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 529-30 (1945).

II. Congress Affirmed Its 1935 Choice To Preserve State Jurisdiction In The 1992 Amendments.

In the 1992 Energy Policy Act amendments to the Federal Power Act, Congress revisited and affirmed the basic political choices made in 1935 on the division between State and Federal regulatory jurisdiction.

On one hand, the 1992 Congress granted FERC authority to order wheeling (unbundled transmission service) on a case-by-case basis. *See* 16 U.S.C. § 824j. In doing so, Congress expressly limited that federal wheeling authority to "*wholesale* transmission services . . . ." 16 U.S.C. § 824k(a) (emphasis added).[7]

On the other hand, the Congress added that FERC has no authority — under any part of the Federal Power Act — to interfere "with any State law which governs the retail marketing areas of electric utilities." 16 U.S.C. § 824k(g).

7. Contrary to Enron's statement (Resp. Br. 37), Congress did not authorize FERC generically to order wheeling "for other users." Rather, it expressly limited FERC's wheeling authorization to wholesale transmission. 16 U.S.C. § 824k(a). Congress also limited the class of persons who could request a wholesale wheeling order to those "generating electric energy for sale for resale." 16 U.S.C. § 824j(a). Contrary to statements made to the Court, Congress did not include "other suppliers and marketers," Enron Resp. Br. 11, or "any person," Pennsylvania PUC *amicus* Br. 6.

Congress further provided that FERC has no authority — again under any part of the Federal Power Act — to order retail wheeling. 16 U.S.C. § 824k(h).

By these provisions, the 1992 Congress affirmed the Federal Power Act's most basic division of jurisdictional authority — that between retail service (which is State-jurisdictional) and wholesale service (which is Federal-jurisdictional). In affirming this jurisdictional division, the 1992 Congress understood that States themselves might provide for retail wheeling (*i.e.*, unbundled retail transmission service, which permits competition for retail power sales):

> New section 212(h) of the Federal Power Act contains a savings clause for State laws dealing with retail wheeling. Thus, State laws that either prohibit or permit retail wheeling are unaffect[ed] by this subsection.

H.R. Conf. Rep. No. 102-1018, at 388 (1992), *reprinted in* 1992 U.S.C.C.A.N. 2472, 2479. Knowing this, Congress nevertheless precluded FERC from issuing retail wheeling orders *even if States permit retail wheeling*. 16 U.S.C. § 824k(h).

Thus, although some parties have argued to the Court that State jurisdiction over unbundled retail transmission is unacceptable from a national perspective, the 1992 Congress decided otherwise. Even where a State provided for retail wheeling, Congress limited its grant of wheeling authority to FERC to "wholesale transmission service." 16 U.S.C. § 824k(a).[8]

---

8. Similarly, although some parties have argued to the Court that protection of a utility's native load customers in preference to (Cont'd)

III. The FERC Decisions TAPS Cites Do Not Show That FERC Regulated "Unbundled Retail Transmission" Before Order 888.

The issue before this Court is whether *FERC* erred in asserting jurisdiction under the Federal Power Act over the rates (and other terms and conditions) of unbundled transmission service purchased by retail customers. TAPS (Br. 38-40) confuses the issue by asserting , based on certain FERC cases involving New York and California, that FERC "has regulated unbundled retail transmission for decades." TAPS is wrong because the cases it cites are, on their faces, inapposite to the issue in this case.

The New York cases TAPS cites all involve transmission service purchased not by a retail customer but by another utility. In *Consolidated Edison Co. of New York*, 15 F.E.R.C. ¶ 61,174 (1981), the Power Authority of the State of New York (PASNY) purchased transmission service for its power from Consolidated Edison. PASNY in turn sold a bundled service to the Port Authority, PASNY's retail customer. In asserting jurisdiction over the PASNY-Con Ed contract, FERC specifically stated that Con Ed's transmission

---

(Cont'd)
others is illicit, the legislative history of the 1992 Act is filled with statements recognizing the necessity (and propriety) of doing so. *See, e.g., 5 Legislative History of the Energy Policy Act of 1992: Senate Comm. on Energy and Nat. Resources*, S. Prt. 103-91, at 3837 (1994) (Rep. Davis); *id.* at 3879-80 (Rep. Kostmayer); *id.* at 3882 (Rep. Oxley); *id.* at 4166 (Rep. Gillmor); *id.* at 4174 (Rep. Eckart); *id.*, Vol. 6 at 4609 (Rep. McMillen) (House bill modified in conference committee better to protect native load customers); *id.* at 4824 (Sen. Johnston); *id.* at 4836-37 (Sen. Wollop) (a utility "owes its primary duty to its native load").

service was "a service provided and billed to PASNY which, in turn, charges its customers." *Id.* at 61,045.

Likewise, *Power Authority of State of New York v. Niagara Mohawk Power Corp.*, 79 F.E.R.C. ¶ 61,159 (1997), and *Niagara Mohawk Power Corp.*, 34 F.E.R.C. ¶ 61,028 (1986), involved a contract for the New York Power Authority (NYPA) (formerly PASNY) to purchase transmission service from Niagara Mohawk.[9] Similarly, the "FERC Rate Schedule 165" in *Niagara Mohawk Power Corp.*, 82 F.E.R.C. ¶ 63,018 (1998), was a "reciprocal arrangement" for Niagara Mohawk and New York State Electric and Gas Company (NYSEG) to purchase transmission service from each other, with Niagara Mohawk receiving a "net payment" from NYSEG and providing "bundled retail generation sales" to its retail customers. *Id.* at 65,136-37.

The California cases TAPS cites are inapposite for a different reason. They all involve a comprehensive 40-year agreement between the Western Area Power Administration, a federal agency, and Pacific Gas and Electric Company (PG&E) to integrate federal government transmission and generation facilities with PG&E's facilities in California for the purpose, *inter alia*, of delivering federally-generated

9. FERC may have used the decision in 1997 — after Order 888 was issued and while the petitions for review in the instant case were pending — as an occasion to imply that the service sold under the NYPA-Niagara Mohawk contract was "unbundled retail transmission service." *See* 79 F.E.R.C. ¶ 61,159 at 61,745. Attaching labels, however, cannot alter or obscure the substance of the contract — wherein "[Niagara Mohawk] hereby agrees to transmit power for [NYPA]," *id.* at 61,746 (brackets by FERC), and "rates [are charged] to . . . NYPA . . . for the transmission of power . . . ." 34 F.E.R.C. ¶ 61,028 at 61,043.

power to federal end-use facilities. FERC's jurisdiction to decide rate issues purportedly is conferred by the terms of the contract between the United States and PG&E, not by any reference to or application of the Federal Power Act. *See, e.g., Pacific Gas & Elec. Co.*, 15 F.E.R.C. ¶ 63,059, at 65,261 (1981) (Initial Wheeling Rate Decision) (quoting Article 32 of Contract 2948A), *modified*, 20 F.E.R.C. ¶ 61,190, at 61,364-65 (1982) (same).

Finally, jurisdictional issues generally were not addressed by FERC in these cases,[10] much less by a court on review. Even decisions by this Court do not decide jurisdictional issues that were not addressed. *Federal Election Comm'n v. NRA Political Victory Fund*, 513 U.S. 88, 97 (1994). "We have often said that drive-by jurisdictional rulings of this sort . . . have no precedential effect." *Steel Co. v. Citizens for a Better Environment*, 523 U.S. 83, 91 (1998). The same should be true of an unreviewed decision of an administrative agency that did not address the jurisdictional issue in the first place. Thus, these inapposite cases TAPS cites have no precedential value in any event.

10. The only exception was *Consolidated Edison*, where FERC ruled that it had jurisdiction because "[t]he entire transaction [between PASNY and Con Ed] comprises a service provided and billed to PASNY which, in turn, charges its customers." 15 F.E.R.C. ¶ 61,174, at 61,045.

CONCLUSION

Citizens Action supports the petitioner State Commissions' position that FERC's orders should be vacated to the extent they assert federal jurisdiction over unbundled retail transmission, contrary to the Federal Power Act both as enacted in 1935 and as amended in 1992.

Respectfully submitted,

MICHAEL A. MULLETT
Counsel of Record
MULLETT & ASSOCIATES
309 West Washington Street
Suite 233
Indianapolis, Indiana 46204
(317) 636-5165

Attorney for Respondent Citizens Action Coalition of Indiana, Inc.

RECEIVED
JUL 6 2001

(20)

Supreme Court, U.S.
FILED
JUL 2 2001
OFFICE OF THE CLERK

No. 00-568

In The
Supreme Court of the United States

People of the State of New York and the Public Service Commission of the State of New York, et al.
Petitioners,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

PETITIONERS' REPLY BRIEF ON THE MERITS

LAWRENCE G. MALONE *
GENERAL COUNSEL

JONATHAN D. FEINBERG
DIANE T. DEAN
ASSISTANT COUNSEL

PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK
THREE EMPIRE STATE PLAZA
ALBANY, NEW YORK 12223-1350
(518) 474-2510

* Counsel of Record

BECKER GALLAGHER LEGAL PUBLISHING, INC.
CINCINNATI, OH 800-890-5001

30 pp

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES iii

I. THE STANDARD OF REVIEW 1

A. FERC's "New Service" Theory 2

B. FERC's Claim To Deference 3

C. FERC's Stare Decisis Argument 4

D. FERC's Post-Hoc Claim Of A Jurisdictional Void 4

II. FERC AND ITS SUPPORTERS HAVE MISREAD THE FPA 5

A. Section 201(a) - "Federal Regulation Of Transmission And Sale of Electric Energy" 5

B. Section 206(d) 8

C. Section 212(h) 9

D. Section 201(b) 10

1. Legislative History 11

2. Case Law 12

III. THE RESPONDENTS' POLICY ARGUMENTS 16

CONCLUSION 20

TABLE OF AUTHORITIES

Cases

Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n, 461 U.S. 375 (1983) 5, 7

Chemehuevi Tribe of Indians v. Federal Power Comm'n, 420 U.S. 395 (1975) 16

Chicago Dist. Elec. Corp., 2 FPC 416 (1941) 13

Cipollone v. Liggett Group, Inc., 505 U.S. 504 (1992) 1, 4, 5

Connecticut Light & Power Co. v. Federal Power Comm'n, 324 U.S. 515 (1945) ..... *passim*

Enron Power Marketing Inc. v. Northern States Power Co., 528 U.S. 1182 (2000) 17

Federal Energy Regulatory Comm'n v. Mississippi, 556 U.S. 742 (O'Connor, J., dissenting) (1982) 18

Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1972) 4, 12, 14, 15

Federal Power Commission v. Southern Cal. Edison Co., 376 U.S. 205 (1964) 8, 16

Food and Drug Admin. v. Brown and Williamson Tobacco Co., 529 U.S. 120, 155-157, 120 S. Ct. 1291 (2000) 4

Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61 (1943) ..... *passim*

Louisiana Public Serv. Comm'n v. Federal Communications Comm'n,
476 U.S. 374 13

Mill Creek Coal v. Public Serv. Comm'n,
100 S.E. 557 (W. Va. 1919) 8

Northern States Power Co. v. Federal Regulatory Energy Comm'n,
176 F.3d 1090 (8th Cir. 1999),
cert. denied, sub nom. 17, 18

Pacific Gas & Electric Company,
1991 FERC LEXIS 2078 at *6-7 3

Procunier v. Navarette,
434 U.S. 555 (1978) 13

Public Utilities Comm'n of Rhode Island v. Attleboro Steam & Elec. Co.,
273 U.S. 83 (1927) 4, 7, 15

United States v. California Public Utilities Comm'n,
345 U.S. 295 (1953) 15

Vance v. Terrazas,
444 U.S. 252 (1980) 13

West Lynn Creamery, Inc. v. Healy,
512 U.S. 186, 114. S. Ct. 2205 (1994) 17

Statutes and Other Authorities

15 U.S.C. § 717f 16
FPA § 201(a) ..... *passim*
FPA § 201(b) ..... *passim*
FPA § 201(c) 13
FPA § 201(e) 10, 12

FPA § 202(f) 20
FPA § 206(d) 8, 9, 11
FPA § 212(a) 9
FPA § 212(h) 9, 10, 11, 15

Curtis, The Law of Electricity, 1-8 (1915) 2

Elsbree, Interstate Transmission of Electric Power,
57-85 (1931) 8

Energy Information Administration/
Annual Review 1999 Table 8.1 (1949-1999) 11

Legislative History of the Energy Policy Act of 1992: Prepared for the Senate Comm. On Energy and Nat. Resources,
103 Cong., 2nd Sess., Vol. 5 at 3837 (1994) 17-18

Randazzo, Has Federal Energy Regulation Collapsed?,
14 Electricity Journal, 11-20 (April 2001) 18

Weiser, Chevron, Cooperative Federalism, and Telecommunications Reform,
52 Vand. L. Rev. 1 (1999) 19

Weiser, Towards a Constitutional Architecture for Cooperative Federalism,
79 N.C.L. Rev. 663 (2001) 19

79th Cong. Rec. 10378 (daily ed. June 28, 1935) 9, 20

H.R. Rep. No. 1318, 74th Cong., 1st Sess. 27 (1935) 5, 8

H.R. 655, 105th Cong., 1st Sess. (1997) 20

"1935 Hearings on H.R. 5423," at 498,
74th Cong., 1st Sess. (1935) 3, 7, 9, 11, 12

"1935 Hearings on S. 1725," at 247 (1935),
74th Cong., 1st Sess. 11, 12

"1947 Hearings on H.R. 2972 and 2973," at 486-487,
80th Cong., 1st Sess. (1947) 4, 11

"1967 Hearings on H.R. 5348," at 124,
90th Cong., 1st Sess. (1967) 3

S. Rep. No. 74-621, at 48 (1935) 12

In defending FERC's attempt to preempt state regulation of retail transmission service, FERC and its supporters implicitly argue that the 1935 Congress inadvertently laid the groundwork for preemption when it authorized FERC to regulate the "transmission of electric energy in interstate commerce" (§ 201(b)). Two factors -- (1) unbundling of the commodity from the rest of the retail customer's bill (FERC 20-21, 39); and (2) added interconnection between utilities (FERC 31-33) -- allegedly transform FERC's § 201(b) authority from permission for FERC to do what the states could not do (regulate transmissions for wholesale transactions) to a license to preempt what the states have always done (regulate retail transmissions). As shown below, the respondents' defense of Order 888 is grounded in (1) an erroneous standard of review; (2) a misreading of the Federal Power Act (FPA); and (3) misplaced policy contentions.

I. THE STANDARD OF REVIEW

The Court will not endorse preemption of fundamental state regulation that preceded an agency's enabling legislation absent a "clear and manifest" showing that it was intended by Congress. Cipollone v. Liggett Group, Inc., 505 U.S. 504 (1992). Order 888 and FERC's brief admit that Congress did not contemplate FERC preempting state regulation of retail transmissions (Joint Appendix, J.A. 347, 593-95; FERC 20, 38-39, 47).

FERC argues, however, that (a) retail transmission service did not exist before unbundling; (b) § 201(b) authorizes FERC to regulate retail transmissions; (c) this Court's decisions support FERC preemption; and (d) if retail transmissions are carried by several utilities across a number of states, only FERC will be able to regulate them (FERC 38-42).

A. FERC's "New Service" Theory

Utilities have delivered (transmitted and distributed) electricity to retail customers since the 1880's (Phillips, "The Economics of Regulation," p. 551 (1969)). In 1935, when the FPA was enacted, Congress knew that the states were regulating retail deliveries and took pains not to disturb their jurisdiction (State Petitioner's Appendix in Support of Petition for Certiorari, Pet. App. L-34). Connecticut Light & Power Co. v. Federal Power Comm'n, 324 U.S. 515, 526 (1945).

FERC contends that retail transmission service, bundled in retail rates for 90 years, became "new" when unbundling of the commodity allowed customers to choose not what company would provide them retail transmission service, but what company would supply their electric energy (FERC 20-21). Retail transmission service has always been a sine qua non of consumers receiving electricity and it has been regulated by the states since the early 1900's. See Curtis, The Law of Electricity, 1-8 (1915). Irrespective of changes in a utility's billing format,[1] retail transmissions take place over the same utility facilities, at the same costs to utilities and, absent FERC preemption, at the same rate for consumers.

Any question as to whether retail transmission service existed in 1935 is answered by this Court's conclusion in Jersey Central Power & Light Co. v. Federal Power Comm'n, 319 U.S. 61, 74 (1943), that § 201(a)'s preservation clause safeguarded state regulation of "transmission." The only transmission to which the Court could have been referring

---

[1] The States' brief established the irrationality and internal inconsistency of FERC's premise that commodity "unbundling" changed the nature of monopoly delivery service (States 27, 35-36). FERC's brief does not answer either point.

was retail transmission because transmissions for wholesale transactions were not subject to state regulation.[2]

B. FERC's Claim To Deference

The States' brief presented several reasons why FERC's reading of the FPA was not entitled to deference (States 16-17). FERC responds that its position deserves deference because Congress could constitutionally preempt retail transmissions (FERC 40 n.20). Congress' ability to preempt retail transmissions is not relevant to whether it has actually done so.

FERC also alleges that its reading of the FPA does not contradict its prior statements to Congress, or the Court. In congressional testimony, FERC has repeatedly stated that the FPA does not allow it to set retail rates. E.g., Hearings before the Committee on Interstate and Foreign Commerce on H.R. 5423, 74th Cong., 1st Sess. (1935), "1935 Hearings on H.R. 5423," at 498; Hearings Before the Subcommittee on Communications and Power of the Committee on Interstate and Foreign Commerce, 90th Cong., 1st Sess. (1967), "1967 Hearings on H.R. 5348," at 124. Its current position -- that the FPA allows it to set retail transmission rates (FERC 39-40) -- contradicts those statements.[3] When a federal agency's reading of a statute

---

[2] In support of an allegation that FERC has regulated unbundled retail transmissions in the past, TAPS cites several FERC decisions that ostensibly regulate retail transmissions (TAPS 38-40). The cases are not relevant because they involved unique facts, such as service to "a critical national defense facility" (Pacific Gas & Electric Company, 1991 FERC LEXIS 2078 at *6-7) and transmission rates that in some instances were set by the states. Further, agency action unreviewed by a court does not establish agency jurisdiction.

[3] FERC accuses the States of asking the Court to write an amendment to the FPA similar to the "Hinshaw Amendment" (FERC 33 n.16). When Congressman Miller, in 1947, introduced a Hinshaw-like amendment in response to state concerns that FERC was

contradicts prior statements to Congress, it does not warrant deference. See Food and Drug Admin. v. Brown and Williamson Tobacco Co., 529 U.S. 120, 155-157, 120 S. Ct. 1291, 1312-1314 (2000).

C. FERC's Stare Decisis Argument

By assuming that Jersey Central, Connecticut Light & Power and Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1972), support its position, FERC argues that it should not have to show that Congress clearly intended to authorize its preemption of retail transmissions (FERC 41). If FERC's interpretation of these holdings were accurate, which is not the case (Point II.D.2), the decisions might offer a basis for satisfying the Cipollone standard. They would not, however, provide a basis for ignoring it.

D. FERC's Claim Of A Jurisdictional Void

FERC contends Cipollone should not apply because if FERC cannot preempt the states, there will allegedly be a jurisdictional void with regard to multi-state retail transmissions (FERC 38-39). Transmissions crossing several states (and various utility service territories) generally involve sales of electric energy for resale. An example would be the sale of energy by Narragansett Electric to Attleboro, which resold to its customers. Public Utilities Comm'n of Rhode Island v. Attleboro Steam & Elec. Co., 273 U.S. 83 (1927). Because such transmissions carry electric energy that will ultimately be distributed by the buyer to the consumer, they are subject to FERC jurisdiction (Point II.A.). If a retail customer were to buy directly from a distant generator and

---

encroaching on state authority, FERC testified that such an amendment was unnecessary because "[t]he field of retail rates ... whether interstate commerce was involved or not was reserved for the States." Hearings Before a Subcommittee of the Committee on Interstate and Foreign Commerce on H.R. 2972 and 2973, 80th Cong., 1st Sess. (1947), "1947 Hearings on H.R. 2972 and 2973," at 486-487.

arrange for multi-state retail delivery through several utility systems, with no intervening purchaser of the energy, the non-discriminatory retail transmission tariffs established by each state would apply (see Point III). See Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n, 461 U.S. 375, 395 (1983) [despite the fact that most retail utilities sell interstate, "the national fabric does not seem to have been seriously disturbed by leaving regulation of retail utility charges largely to the States"]. There would be no jurisdictional void.

Order 888 is an extraordinary example of an administrative agency attempting to use circumstances that, under its own preemption theory, were not envisioned by Congress (FERC 20-21) to supplant state regulation that Congress insisted "was not [to be] disturbed." H.R. Rep. No. 1318, 74th Cong., 1st Sess. 27 (1935). It does not pass muster under Cipollone.

II. FERC AND ITS SUPPORTERS HAVE MISREAD THE FPA

A. Section 201(a) - "Federal Regulation Of Transmission And Sale Of Electric Energy"

Section 201(a) describes two sides of the same coin. The first side sets forth the scope of federal interest and federal regulation. The second side defines what FERC may not regulate.

Side one declares a federal interest in "the business of transmitting and selling electric energy," not for consumption, but "for ultimate distribution to the public." It then states that FERC may regulate generation, under limited circumstances, and "that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce." For several reasons, side one of § 201(a) has to be read as limiting FERC's jurisdiction to transmissions for wholesale transactions.

First, the transmissions being regulated by FERC are part of a "business" that transmits and sells energy not for consumption, but for "ultimate distribution" by the buyer to the public. Inasmuch as the initial buyer of such energy resells, rather than consumes, it, the transmission to that buyer for "ultimate distribution to the public" (another sale) is a transmission for a wholesale sale.

Second, if there is any question whether the "business" described in the introductory clause (transmitting and selling energy "for ultimate distribution to the public") is a wholesale business, the matter is resolved by side one's language limiting FERC's jurisdiction to the sales for resale and associated transmissions by that business. By specifying that FERC would regulate the "transmission of electric energy in interstate commerce and the sale of such [transmitted] energy at wholesale in interstate commerce ...," Congress left no question that the universe of transmissions subject to FERC regulation was limited to transmissions of energy sold at wholesale ["the sale of such [transmitted] energy at wholesale"].[4]

FERC's position that § 201(a)'s statement of federal interest "confirms that the Commission has jurisdiction over ... interstate transmission of energy (whether for wholesale or retail sales)" (FERC 20, 34) is incorrect. One in "the business of transmitting and selling electric energy for ultimate distribution to the public" is in a wholesale business. In allowing FERC to regulate the part of that business that transmits energy to be sold at wholesale, Congress

[4] In attempting to distinguish § 201(a)'s reference to "the transmission of electric energy in interstate commerce" from "the sale of such energy at wholesale in interstate commerce" (TAPS 19), TAPS simply loses sight of the fact that the "such energy" language of the second phrase qualifies the energy over which FERC has transmission jurisdiction.

unequivocally limited FERC's jurisdiction to transmissions for wholesale transactions.

The flip side of § 201(a) provides that federal regulation cannot extend to matters subject to regulation by the states. The Court in Jersey Central, 319 U.S. at 74-75 (1943), noted that § 201(a)'s preservation clause "is directed at ... transmission." Side two like side one, therefore, prohibits FERC from regulating retail transmissions, which were -- by FERC's testimony in 1935 -- a matter subject to rate regulation by the states (1935 Hearings on H.R. 5423 at 556).

FERC's insistence that § 201(a)'s preservation clause "cannot nullify a clear and specific grant of jurisdiction" (FERC 34) is a red herring. Section 201(a)'s federal interest applies only to transmissions for wholesale transactions and, as FERC admits, "Section 201(a) states the same rule as Section 201(b)" (FERC 34). In safeguarding the states' pre-existing retail transmission jurisdiction, therefore, § 201(a)'s preservation clause does not conflict with a grant of jurisdiction to FERC.

Perhaps recognizing that § 201(a)'s plain language preserves state jurisdiction of all retail transmissions, EEI incorrectly contends that even if § 201(a) reflects "a policy of giving the States jurisdiction over any area that they could regulate," the states were barred by the Commerce Clause in 1935 (as interpreted in Attleboro) from regulating retail transmissions in interstate commerce (EEI 23-24). Attleboro held that because Rhode Island's regulation "involved a transaction at wholesale, it imposed a direct rather than an indirect burden on interstate commerce" (emphasis added). Arkansas Elec. Coop., 461 U.S. at 378 (1983). The Court did not express concern with state regulation of retail

transmissions.[5] See Elsbree, Interstate Transmission of Electric Power, 57-85, 99 (1931).

B. Section 206(d)

At the risk of stating a truism, rates that recover retail transmission costs are, or include, retail transmission rates. The States' brief noted that (a) § 206(d) assumes that retail rates set by state commissions recover interstate retail transmission costs and (b) FERC's brief in Connecticut Light & Power, acknowledged this point. FERC Brief of December 1944, pp. 28-29, citing in part H. Rep. No. 1318, 74th Cong., 1st Sess., p. 29 (States 24, 40).

Respondent Enron argues that FERC's brief "acknowledges only that states have jurisdiction over the rates for 'sale to the ultimate consumer'" (Enron 28 n.17). FERC, and Congress, would not have cited FERC's provision of interstate transmission costs to the states if they had envisioned state ratemaking jurisdiction being limited to the commodity.[6] Indeed, as indicated, Congress was aware that

---

[5] The Court cited Mill Creek Coal v. Public Serv. Comm'n, 100 S.E. 557 (W. Va. 1919), to establish that transmissions for wholesale transactions across state lines were in interstate commerce, not -- as EEI seems to imply -- to question the ability of states to regulate interstate retail transmissions. 273 U.S. at 86. As discussed below, the Court in Federal Power Commission v. Southern Cal. Edison Co., 376 U.S. 205 (1964) rejected a contention that a new reading of the Commerce Clause would diminish FERC jurisdiction under the FPA. It did not hold, however, as EEI implies, that retrospective readings of the Commerce Clause were relevant to the FPA's meaning.

[6] In explaining § 206(d)'s reference to transmission costs, FERC Solicitor DeVane stated the Commission would provide state regulators with the costs of out-of-state transmission lines. (Pet. App. L-24). When asked by Congressman Lea, "would that be with the idea of affording the state commissions ample information upon which to base rates?", Mr. DeVane answered: "Yes, sir" (Pet. App. L-

the bulk of the retail customer's bill recovered the utility's delivery costs (1935 Hearings on H.R. 5423 at 556).

Sections 201(a), 206(d) and repeated statements from FERC and the Congress demonstrate that Congress did not intend FERC to regulate retail deliveries (e.g., 79th Cong. Rec. 10378 (daily ed. June 28, 1935) [wherein Congressman Lea concluded that "the Federal Power Commission does not fix the rate of delivery" in a retail transaction]). Congress did intend, however, that state regulated, retail rates would recover interstate, retail transmission costs (Id.). Order 888 nullifies Congress' intention.

C. Section 212(h)

In 1992, Congress empowered FERC to require wholesale, not retail, wheeling (§ 212(a)) and directed that "[n]othing in this subsection shall affect ... State law concerning the transmission of electric energy directly to an ultimate consumer." The States' initial brief pointed out that Congress in 1992 would not have safeguarded state regulation relating to retail transmissions if it had already authorized FERC to preempt such regulation (States 36). Rather than attempt to reconcile its expansive reading of § 201(b) (discussed below) with § 212(h)'s explicit prohibition of preemption, FERC insists that it did not violate § 212(h)'s directive against mandatory retail wheeling (FERC 36-37). No party has suggested that FERC ordered retail wheeling, but FERC has preempted state laws that direct state commissions to regulate retail transmission service.

TAPS argues that § 212(h) simply preserves the discretion of states not to require utilities to transmit competitors' electricity to retail customers and then speculates that there would have been no need to provide such protection unless Congress, in § 201(b), had established

---

25).

FERC's jurisdiction to regulate retail transmissions (TAPS 26-29). Its argument is inconsistent with FERC's acknowledgment that § 201(b) did not empower it to order retail wheeling. If FERC was not empowered in 1992 to order retail wheeling, then § 212(h) had to reflect Congress' intention to safeguard "State law concerning the transmission of electric energy directly to an ultimate customer." Order 888 preempts a portion of such laws.

D. Section 201(b)

Because electric energy, like any commodity, is either consumed or resold, § 201(a)'s and (b)'s references to sales of "energy at wholesale" clearly define FERC's commodity jurisdiction. Energy transmission, like any delivery service, is a prerequisite to a retail or wholesale sale of the commodity, but, unlike a commodity, it is not consumed or resold. In order to permit meaningful regulation of wholesale and retail transactions, Congress, therefore, delineated federal/state transmission jurisdiction in terms of the specific transaction being effectuated, with transmissions for "the sale of . . . energy at wholesale" (§ 201(a)) being FERC jurisdictional and transmissions "directly to an ultimate customer" (§ 212(h)) being state jurisdictional.

The respondents claim that § 201(b) assigns FERC jurisdiction of all transmissions because "wholesale" does not appear before "transmission" in the first clause (FERC 24). As indicated, placing "wholesale" before transmission in § 201(b) would have drawn more questions than answers. For example, because the second sentence of § 201(b) refers to the transmission described in clause 1 in granting FERC jurisdiction over facilities (for "such transmission") and § 201(e) defines public utilities as companies that own facilities subject to FERC's jurisdiction, inserting "wholesale" before "transmission" in § 201(b)'s first clause would have reduced the companies subject to FERC jurisdiction.

When read together, clauses 1 and 2 of § 201(b) provide FERC jurisdiction to encourage interconnection and to fulfill its § 206(d) obligation to facilitate the states' setting of retail rates. Section 201(b) states the same rule as § 201(a) (FERC 42), and § 201(a) denies FERC jurisdiction of retail transmissions. FERC's reading of § 201(b) places it in conflict with not only § 201(a), but §§ 206(d) and 212(h).

1. Legislative History

The States' initial brief cited legislative history that demonstrated Congress' intent to preserve pre-existing state jurisdiction over retail deliveries (States 18-33). The respondents argue that the history refers only to state jurisdiction over retail commodity sales (FERC 37-39).

At the 1935 Hearings on the FPA, FERC testified that the states were regulating retail deliveries (Hearings on H.R. 5423 at 556) and that the FPA took no authority from the states (Pet. App. L-34). Twelve years later, FERC reiterated that it had no authority over retail rates. See 1947 Hearings on H.R. 2972 and 2973 at 486, 489. In 1967, FERC Chairman White testified that "this State [retail] function covers more than 90 percent of the electric revenues of jurisdictional public utilities" (Pet. App. H-14). In order for Chairman White's "more than 90 percent" statement to have been accurate, it had to have included retail transmission revenues. Energy Information Administration/Annual Review 1999 Table 8.1 (1949-1999).

Enron and FERC contend that the states have misstated relevant legislative history by citing a statement by Solicitor DeVane, but omitting a clause (FERC 32; Enron 27). The quotation of Solicitor DeVane that is challenged by FERC and Enron, upon reflection, was inapt, but not for the reasons argued by FERC and Enron (the exclusion of "unless they are also a part of the facilities that are used in interstate commerce" (FERC 32; Enron 27)). The language cited was not relevant because it concerned a legislative provision that was

not adopted and -- in any event -- addressed FERC's jurisdiction over companies, not services. See Pet. App. L-30 through L-36.

The FPA's legislative history establishes that FERC's rate jurisdiction does not include retail transactions (S. Rep. No. 74-621, at 48 (1935)). Accord, e.g., id. at 20, 51; Hearings Before the Senate Committee on Interstate Commerce on S. 1725, 74th Cong., 1st Sess., "1935 Hearings on S. 1725," at 247 (1935) (section-by-section analysis); id. at 268; 1935 Hearings on H.R. 5423 at 386 (section-by-section analysis). FERC and its supporters have not only failed to refute this history, but have pointed to no evidence of a congressional intent that if the retail commodity was unbundled from retail delivery service, then jurisdiction over the transmission element of retail deliveries would shift to FERC.

2. Case Law

FERC and its supporters contend that this Court's decisions in Jersey Central, 319 U.S. 61, Connecticut Light & Power, 324 U.S. 515 and Florida Power & Light, 404 U.S. 453, establish that all transmissions are in interstate commerce and "provide 'cardinal and guarding' interpretations of Sections 201" (FERC 40-41). Inasmuch as Congress preserved the states' jurisdiction of all retail transmissions, the respondents' attempted use of the cases is misplaced, as well as incorrect.

In Jersey Central, the Court held that because some energy generated by Jersey Central arrived in New York State from an intervening company's transmission lines, Jersey Central was a public utility under § 201(e) and its stock purchases were subject to FERC jurisdiction. The case affirms that (a) although a company may be a public utility under subsection (e), all of its transactions do not thereby fall under the regulatory power of the Commission (319 U.S. at 73); and (b) while § 201(a)'s preservation of pre-existing state regulation naturally could not override the FPA's explicit delegation to FERC of jurisdiction over Jersey Central's

financial arrangements, it did apply to "generation, transmission and sale" (emphasis added) (319 U.S. at 74).

Connecticut Light & Power held that FERC lacked jurisdiction over a company unless the company's facilities were used for interstate transmission (as opposed to distribution) of electric energy (324 U.S. at 522). Because the FPA denies FERC jurisdiction over retail transmission service (including interstate retail transmissions), the Court need not determine when a particular transmission is in interstate commerce.[7] If, however, the Court determines that the states may only regulate intrastate retail transmissions, then, as Connecticut Light & Power noted, § 201(c)'s definition of such transmissions would control.[8]

---

[7] FERC, TAPS and EEI contend that the states have altered their position from the D.C. Circuit insofar as they argue that the FPA preserves the states' jurisdiction over all retail transmissions, as opposed to simply intrastate retail transmissions (FERC 28). The wording of the States' questions for certification does not preclude the States from establishing that the FPA safeguarded the states' jurisdiction over all retail transmissions, including those in interstate commerce. If FERC cannot preempt any retail transmissions, it certainly cannot preempt intrastate retail transmissions and, therefore, the respondents' claims regarding a change of position go solely to the scope of a remedy on remand. See Procunier v. Navarette, 434 U.S. 555, 559-560, n.6 (1978); Vance v. Terrazas, 444 U.S. 252, 258-259 (1980). Moreover, even as to a FERC decision on remand, a federal agency must abide by its jurisdictional limitations, irrespective of the wording of prior jurisdictional claims. Louisiana Public Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. at 374 ["an agency literally has no power to act, let alone preempt the validly enacted legislation of a sovereign state, unless and until Congress confers power upon it"].

[8] See Chicago Dist. Elec. Corp., 2 FPC 416 (1941) [wherein FERC concluded the supplying of electric energy by one company to another, whose operations were entirely in the same state, did not involve a transmission of electric energy in interstate commerce as defined in § 201(c) of the Federal Power Act, even though a portion

Enron mischaracterizes the Court's decision in Connecticut Light & Power, by claiming that the Court adopted "an engineering and scientific, rather than a legalistic or governmental test . . . ." Enron 18. In support of its allegation, Enron quotes a statement from the decision relating to a bill that FERC had proposed. Enron does not point out, as did the Court, that Congress amended the bill to protect state jurisdiction (324 U.S. at 529). In language particularly applicable to the brief of amicus curiae physicists (discussed below), the Court stated "state lines and boundaries cut across and subdivide what scientifically or economically viewed may be a single enterprise. Congress . . . sometimes is moved to respect state rights and local institutions even when some degree of efficiency of a federal plan is sacrificed." Id. at 530.[9]

FERC contends that Florida Power & Light stands for the proposition that all retail transmissions are in interstate commerce because the Court rejected the utility's claim that none of Florida Power & Light's power was in interstate commerce (FERC 33). The holding that one or more of the electrons transmitted in Florida Power& Light's transmission lines were in interstate commerce does not support an induction that all electrons transmitted by interconnected companies are in interstate commerce.[10]

---

of the electric energy so supplied went to another state and then re-entered the original state without any such electric energy being taken or used within the second state.

[9] Electric customers are normally not served by a single pool of random energy (the "theory of unified electric response") except under abnormal or transient conditions (Phys. 15-17). Electric service is continuously monitored by system operators who balance energy flows within control areas (Eng. 23) and direct power flows from generators to load. J.A. 836-839. (See Point III.)

[10] FERC also mistakes jurisdiction over companies for jurisdiction over services when it cites Justice Douglas' dissent as supporting its position. Justice Douglas was, perhaps, prescient of FERC's craving

FERC assured this Court in Florida Power & Light that the case involved whether a particular utility fell within FERC's jurisdiction. FERC Petition for Writ of Certiorari to the United States, November, 1970, p. 10; FERC Brief on the Merits, May, 1971, p. 20. Its claim today that Florida Power & Light supports its attempt to regulate retail transmission rates contradicts its prior position (See Pet. H-31).

FERC also cites the Court's decision in United States v. California Public Utilities Comm'n, 345 U.S. 295 (1953) as supporting a broad reading of its § 201(b) jurisdiction (FERC 34). In determining whether FERC's jurisdiction under the FPA included rate regulation of wholesale commodity sales, the Court in United States v. CPUC focused on the Act's legislative history, reiterated that it was Congress' intent to fill the Attleboro gap (while preserving pre-existing state regulation) and concluded that FERC's jurisdiction extended to wholesale sales. 345 U.S. at 307-311. The holding provides no support for FERC's position in this case.

There simply is no case law that supports FERC Order 888 because the FPA preserved pre-existing state regulation and did not assign FERC jurisdiction of retail transmission service.[11]

---

for greater authority when he stated " . . . the Congress promised that as much as possible be left to the States, I would not make that a hollow promise . . . the federal camel has a tendency to occupy permanently any state tent" (404 U.S. at 470). However, his observation that the majority's holding would render every privately owned interconnected facility subject to FERC's jurisdiction does not support FERC's attempt to regulate retail transmission service (FERC 32-33).

[11] The respondents cite decisions under the Natural Gas Act (NGA), but -- as indicated in the States' May 2001 brief -- the decisions are not relevant because -- among other things -- the NGA does not include an equivalent to §§ 201(a) or 212(h) (States 12-16). Indeed, under the NGA, FERC has the authority to approve and regulate

III. THE RESPONDENTS' POLICY ARGUMENTS

Enron, FERC and other respondents argue at length that because of increased interconnection all electricity on the interconnected grid is in interstate commerce. (FERC 26; Enron 21). While the 1935 Congress empowered FERC to encourage interconnection in order to facilitate regional coordination, it did not even insinuate an inverse relationship wherein increased interconnection would decrease state jurisdiction over retail services. See Federal Power Comm'n v. Southern Cal. Edison Co., 376 U.S. 205, 213-217 (1964) [which noted that FERC's jurisdiction was set by Congress in 1935 and could be neither increased nor decreased without congressional action]. Increased interconnection does not alter jurisdictional lines. See Chemehuevi Tribe of Indians v. Federal Power Comm'n, 420 U.S. 395, 422-423 (1975).

The respondents TAPS and Enron allege that if FERC is not permitted to supplant state regulation of retail transmissions, utilities will provide discriminatory transmission service (TAPS 34-35; Enron 39-41, 43). FERC does not have to preempt state regulation of retail transmission service in order to assure nondiscriminatory access to transmissions associated with wholesale transactions. When the Circuit Court upheld FERC's wholesale open access Order, nondiscriminatory transmissions for wholesale transactions became required by law. FERC's ability and willingness to enforce its Order will determine the openness of transmissions for wholesale transactions.[12]

---

certification, construction and abandonment of gas transmission facilities. 15 U.S.C. § 717f. Under the FPA, by contrast, FERC has no such authority. Thus, FERC has traditionally regulated 90% of the gas industry, but only 15% of the electric industry.

[12] State regulation, as indicated in the States' May, 2001 brief in 00-809, is more than capable of addressing utility discrimination against retail providers (States 18-22) and will provide a healthy supplement

Enron also alleges that state regulation of retail transmission is "a recipe for state-against-state discrimination" (Enron 3, 14-16, 41-42).[13] Its claim is belied by not only history, but accelerated efforts at the state level to assure cooperation.[14] If one or more states discriminate against out-of-state suppliers (or out-of-state consumers), corrective action is available under the Commerce Clause (see West Lynn Creamery, Inc. v. Healy, 512 U.S. 186, 114. S. Ct. 2205, 2215-6 (1994)). Nearly all states realize it would be shortsighted to exclude competitors' electricity, and thereby deny their own consumers (and economies) opportunities for economic growth.

The Pennsylvania Public Utility Commission contends that Northern States is "manifestly erroneous" and that FERC preemption is necessary to counter parochial state interests, such as those safeguarded by the Eighth Circuit (Pa 8-9).[15] At

---

to federal efforts.

[13] As an alleged example of state "discrimination," Enron points to California's statement that states commonly require electric utilities to protect retail customers during capacity constraints (Enron 41-42). Enron's claim is simply an attempt to relitigate the arguments it unsuccessfully raised in Northern States Power Co. v. Federal Regulatory Energy Comm'n, 176 F.3d 1090 (8th Cir. 1999), cert. denied, sub nom., Enron Power Marketing Inc. v. Northern States Power Co., 528 U.S. 1182 (2000).

[14] E.g.: NECPUC: New England Conference of Public Utilities Commissioners, Inc.; MACRUC: Mid-Atlantic Conference of Regulatory Utilities Commissioners; MARC: Mid-America Regulatory Commissioners; SEARUC: Southeastern Association of Regulatory Utility Commissioners; WCC: Western Conference of Public Service Commissioners. The states of these regions have developed these coalitions to address multi-state issues in a manner that assures coordination while recognizing local conditions.

[15] Northern States upheld the states' (and presumably the nation's) priority of safeguarding native load. See, e.g., Legislative History of

FERC, the Pennsylvania PUC just as vehemently opposed FERC preemption of retail transmission service, stating that "FERC is impermissibly attempting to expand its jurisdiction, not by virtue of new statutory authority, but by an impermissibly broad and technically insupportable re-definition of existing statutory authority" (Pennsylvania PUC Petition for Rehearing dated May 23, 1996 at 27). Pennsylvania never explains its change of position or why it assumes that states that have unbundled to promote retail competition would decide to impede competition by sabotaging the wholesale system. Its arguments are implausible.

The United States has benefitted considerably from the use of states as national laboratories. Federal Energy Regulatory Comm'n v. Mississippi, 556 U.S. 742, 788 (O'Connor, J., dissenting) (1982). A one-size-fits-all policy for transitioning to competitive retail electricity markets -- developed by a single, ill-equipped regulatory agency[16] -- is a recipe for a diminution of service, unnecessarily high rates and unresolved customer complaints.

Respondent Enron alleges that FERC preemption of retail transmission is needed to ensure uniform transmissions across state borders (Enron 39-40). Although Order 888 has been in effect for several years, transmission continues to be state-specific due to unique local and regional conditions, including transmission limitations between states, as well as the isolation of the eastern and western interconnections from each other and the Texas grid. Order 888 has impeded the development of new transmission capacity because the FERC transmission rate formula does not recover new transmission

---

the Energy Policy Act of 1992: Prepared for the Senate Comm. On Energy and Nat. Resources, 103 Cong., 2nd Sess., Vol. 5 at 3837 (1994).

[16] Randazzo, Has Federal Energy Regulation Collapsed?, 14 Electricity Journal, 11-20 (April 2001).

capital costs, except when paid for by marketers or to prevent grid failure. Further, although the States have every incentive to encourage new transmission facilities, and transmission innovation, their ability to do so is diminished by FERC's control of retail transmission rates. For example, in some regions, depending on transmission configurations, new technologies can substantially increase the efficiency of available transmission facilities and thereby reduce the need for new electric generation facilities. The installation of such equipment requires retail transmission rate designs that encourage investment by rewarding increased efficiency. Order 888 defeats the ability of states to design such rates.[17]

The respondents' suggestion that continuing the states' pre-Order 888 regulation of retail transmission rates would impede the operation of the grid ignores the proven ability of computer programs to accommodate multi-state operations.[18] Each state will continue to have retail transmission rates on file that will be applied, by computer program, to particular transactions just as transactions today reflect the FERC Open Access Transmission Tariff (OATT) in some instances and not

---

[17] FERC largely ignored the states' policy observations (States 46-48), arguing that states would retain authority over local reliability and customer service (FERC 42). FERC-induced, as opposed to statutorily designed, split regulation of local services invites long-term problems. See Weiser, Chevron, Cooperative Federalism, and Telecommunications Reform, 52 Vand. L. Rev. 1 (1999); Weiser, Towards a Constitutional Architecture for Cooperative Federalism, 79 N.C.L. Rev. 663 (2001).

[18] For decades prior to FERC's issuance of Order 888, two multi-state power pools adhered to a computer program that called for a sharing of energy between various utilities with automatic billing mechanisms that assured equity and the usage of the least expensive generation at any moment in time to meet marginal demand on the network. The New York Power Pool oversaw a similar arrangement among New York's seven utilities. States are currently discussing the widespread application of such models on regional bases.

in others (depending upon whether a rate in a particular state is bundled).

Congress would not have safeguarded state regulation of delivery rates when energy crosses state lines if it had been concerned with the states' ability to regulate interstate transmissions (79 Cong. Rec. 10378 [daily ed. June 28, 1935]). In fact, inasmuch as Congress assigned the states jurisdiction of transmissions for wholesale transactions across international borders (§ 202(f)), it clearly preferred state regulation of transmissions when constitutionally permissible.

CONCLUSION

The FPA was explicitly designed not to preempt state law (FERC 38). Congress, well aware of the stresses and strains on the FPA's regulatory scheme in recent years, has not changed the Act.[19] In attempting to jerry-build a rationale for new jurisdictional lines, FERC has subverted the will of Congress. Order 888, insofar as it preempts state regulation of retail transmission service, should be annulled.

Respectfully submitted,

Lawrence G. Malone*
General Counsel

Jonathan D. Feinberg
Carl F. Patka
Diane T. Dean
Carol E. Coyne
Assistant Counsel

---

[19] Congress was asked annually from 1997-2000 to authorize FERC regulation of retail transmission service, but did not do so. See, e.g., H.R. 655, 105th Cong., 1st Sess. (1997).

New York State Department
of Public Service
Public Service Commission
Three Empire State Plaza
Albany, New York 12223-1350
(518) 474-2510

*Counsel of Record

July 2001

James Bradford Ramsay
General Counsel
Sharla Barklind
Assistant General Counsel
National Association of Regulatory
Utility Commissioners
1101 Vermont Avenue, Suite 200
Washington, D.C. 20005

Catherine D. Bedell
General Counsel
Richard Bellak
Associate General Counsel
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Alan G. Lance, Attorney General
Donald L. Howell, II, Deputy Attorney General
Idaho Public Utilities Commission
472 W. Washington Street
P.O. Box 83720
Boise, ID 83720-0074

John J. Farmer, Jr.
Attorney General, State of New Jersey
Helene S. Wallenstein, Senior Deputy
Attorney General
Attorney for New Jersey Board of
Public Utilities
124 Halsey Street, 5th Floor
P.O. Box 45029
Newark, NJ 07101

Jo Anne Sanford
North Carolina Utilities Commission
Robert P. Gruber, Public Staff, North Carolina
Utilities Commission
Gisele L. Rankin, Staff Attorney
P.O. Box 29520
Raleigh, NC 27626-0520

William H. Chambliss, General Counsel
C. Meade Browder, Jr., Associate General Counsel
Virginia State Corporation Commission
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218

Christine O. Gregoire, Attorney General
William Berggren Collins, Senior Assistant
Attorney General
Robert D. Cedarbaum, Senior Counsel
(for the Washington Utilities and
Transportation Commission)
P.O. Box 40128
Olympia, WA 98504-0128

Harvey L. Reiter
(for the Vermont Department of Public Service)
Morrison & Hecker
1150 18th Street, N.W., Suite 800
Washington, D.C. 20036

Harry Ivey
(for the Wyoming Public Service Commission)
Attorney General's Office
State of Wyoming
123 Capitol
Cheyenne, WY 82002

Apr 19, 2001 (9)

No. 00-568

Supreme Court, U.S.
FILED
APR 19 200
CLERK

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK and THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF *AMICI CURIAE* THE STATE OF CALIFORNIA AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA IN SUPPORT OF PETITIONERS

BILL LOCKYER
Attorney General of the State of California
PETER SIGGINS
Chief Deputy Attorney General
RICK FRANK
Chief Assistant Attorney General
MORRIS BEATUS
Senior Assistant Attorney General
1300 I Street, Suite 125
Sacramento, CA 94244-2550
(916) 445-1939

GARY M. COHEN*
General Counsel
WILLIAM JULIAN II
PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA
505 Van Ness Avenue
San Francisco, CA 94102
(415) 703-1086

**Counsel of Record*

Attorneys for Amici Curiae the State of California and the Public Utilities Commission of the State of California

166594

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

39 pp

QUESTION PRESENTED

Whether States surrender their jurisdiction over retail transmission to the Federal Energy Regulatory Commission ("FERC"), changing the jurisdictional lines established by the Federal Power Act, if they permit retail customers to choose a power supplier different from the retail transmission supplier.

TABLE OF CONTENTS

	Page
Question Presented	i
Table of Contents	ii
Table of Cited Authorities	iv
Interest of the *Amici Curiae*	1
Summary of Argument	2
Argument	4
I. FERC's Claim Of Jurisdiction Over Retail Transmission Is Contrary to the Purpose of the Federal Power Act, its Legislative History, the Statutory Language and this Court's Decisions.	4
A. The States Have Always Had Jurisdiction Over Retail Transmission, Because the Purpose of the Federal Power Act Is to Preserve State Jurisdiction.	4
B. The Case Law and the Legislative History Dispositively Establish That "Local Distribution" Is a "Part" of Transmission in Interstate Commerce That Section 201 Withholds From FERC's Jurisdiction.	7
C. The Case Law and the Legislative History Dispositively Establish That "Local Distribution" Under Section 201 Includes Retail Transmission.	13

Contents

	Page
D. The Scope of FERC's Jurisdiction is Established by Statute and is not a Factual Inquiry.	18
E. FERC's Jurisdictional Analysis Misuses This Court's Precedents.	22
II. FERC's Construction Of Section 201 Is Not Entitled to Deference.	25
III. The Consequences Of FERC's Assertion Of Jurisdiction Over Retail Transmission Are Terribly Intrusive Of State Regulatory Authority.	27
Conclusion	30

TABLE OF CITED AUTHORITIES

Page

Cases:

Allentown Mack Sales and Serv., Inc. v. NLRB, 522 U.S. 359 (1998) 19, 20

Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n, 461 U.S. 375 (1983) 4, 13, 14, 16, 22

California Power Exch. Corp., 1998 FERC LEXIS 2361 (Nov. 24, 1998) 28

Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) 25, 26

Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) ..... *passim*

East Ohio Gas Co. v. Tax Comm'n, 283 U.S. 465 (1931) 24, 25

FPC v. East Ohio Gas Co., 338 U.S. 465 (1950) .. 22, 24

FPC v. Florida Power & Light Co., 404 U.S. 453 (1972) 22, 23, 25, 30

FPC v. Southern California Edison Co., 376 U.S. 205 (1964) 4, 5, 10, 14, 18, 19, 23

General Motors Corp. v. Tracy, 519 U.S. 278 (1997) 24, 28

Page

Jersey Central Power & Light Co. v. FPC, 319 U.S. 61 (1943) 10, 22, 23, 25

Missouri v. Kansas Gas Co., 265 U.S. 298 (1924) 4, 13, 14, 15, 16, 22

Northern States Power Co. v. FERC, 176 F.3d 1090 (8th Cir. 1999), *cert. denied sub nom. Enron Power Mktg., Inc. v. Northern States Power Co.*, 528 U.S. 1182 (2000) 29, 30

Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) 29

Panhandle Eastern Pipe Line Co. v. Michigan Public Serv. Comm'n, 341 U.S. 329 (1951) 13, 24

Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n of Indiana, 332 U.S. 507 (1947) 10, 13, 14

Pennsylvania Gas Co. v. Public Service Comm'n, 252 U.S. 23 (1920) 9, 10, 15, 16, 17, 24, 25

Public Utils. Comm'n of R.I. v. Attleboro Steam & Elec. Co., 273 U.S. 83 (1927) ..... *passim*

San Diego Gas & Elec. Co. v. Sellers of Energy, 93 FERC ¶ 61,121 (2000), 93 FERC & 61,294 (2000) 27, 28

South Carolina Power Co. v. South Carolina Tax Comm'n, 52 F.2d 515 (E.D. S.C. 1931), *aff'd mem.*, 286 U.S. 525 (1932) 8

Page

Southern Nat. Gas. Corp. v. Alabama, 301 U.S. 148 (1937) 25

United States v. Public Utils. Comm'n of California, 345 U.S. 295 (1953) 5, 14, 15, 23

Utah Power & Light Co. v. Pfost, 286 U.S. 165 (1932) 8

Statutes:

16 U.S.C § 824 ..... 8, 11, 13, 15, 16, 18, 25

16 U.S.C § 824a 25, 26

16 U.S.C. § 824a(b) 29

16 U.S.C § 824a(b)-(d) 18

16 U.S.C. § 824(b) 23

16 U.S.C. § 824(b)(1) 7, 8, 11, 13, 15, 16, 17, 18, 23

16 U.S.C. § 824e(d) 17

16 U.S.C. § 824f 29

16 U.S.C. § 824k(g)-(h) 20

Cal. Pub. Util. Code § 334 27

Cal. Pub. Util. Code § 335 27

Cal. Pub. Util. Code §§ 345 *et seq.* 27

Cal. Pub. Util. Code § 348 27

Page

Other Authorities:

59 Fed. Reg. 35274 (July 11, 1994) 29

3 F.E.R.C. Stats. & Regs., ¶ 31,048 19

To Provide for Control in the Public Interest of Public Utility Holding Companies Using the Mails and the Facilities of Interstate Commerce, to Regulate the Transmission and Sale of Electric Energy and Natural Gas in Interstate and Foreign Commerce, and for Other Purposes:Hearings on H.R. 5423 Before the House Comm. On Interstate and Foreign Commerce, 74th Cong. (1935) ("1935 House Hearings") 5, 8, 10, 15, 16, 17, 19

H.R. Rep. No. 74-1318 (1935) ("1935 House Report") 5, 17, 18

S. Rep. No. 74-621 (1935) ("1935 Senate Report") 5, 8, 15, 16, 18, 29

To Provide for the Control and Elimination of Public Utility Holding Companies Operating, or Marketing Securities, in Interstate and Foreign Commerce and through the Mails, to Regulate the Transmission and Sale of Electric Energy in Interstate Commerce, to Amend the Federal Water Power Act, and for Other Purposes: Hearings on S. 1725 Before the Senate Comm. On Interstate Commerce, 74th Cong. (1935) ("1935 Senate Hearings") 5, 8, 10, 11, 15, 17, 29

S. Rep. No. 817, 83d Cong., 1st Sess. (1953) 24

INTEREST OF THE *AMICI CURIAE* [1]

As part of a now notorious electric utility deregulation experiment begun in the mid-1990s, California effectively ceded to FERC regulatory jurisdiction over the retail transmission facilities of the State's three large investor-owned electric utilities. As a consequence, *amici curiae* the State of California and Public Utilities Commission of the State of California ("CPUC") have first-hand experience with regulatory conflicts and retail service difficulties that result when a State loses its retail transmission jurisdiction to FERC. Our unique interest concerns California's ongoing efforts to resolve the electric utility disaster caused by retail restructuring. FERC's erroneous jurisdictional claim imposes significant constraints on California's regulatory alternatives in pulling back from the precipice.

The State of California and CPUC support the petitioner State and State Commissions' position that FERC's jurisdictional claim is erroneous and its Order 888[2] should be vacated. FERC may say, correctly, that California previously acknowledged FERC's jurisdiction over unbundled retail transmission, and now is changing its mind about changes in jurisdictional lines. Harsh experience has a way of changing minds. Here as elsewhere, it is better that wisdom come late than not at all; and that, by returning to the regulatory system Congress enacted, Sister States may benefit from "lessons in regulation . . . learned by trial and error . . . without involving a

1. **Rule 37.6 Statement.** Stanley C. Fickle, who serves as special counsel for the Public Utilities Commission of the State of California ("CPUC") in a range of litigation matters, authored large portions of this brief. Mr. Fickle is also counsel for Indianapolis Power & Light Company, an inactive party before this Court. No person or entity other than the CPUC made a monetary contribution to the preparation or submission of this brief.

2. Order No. 888, F.E.R.C. Stats. & Regs., Regulations Preambles, January 1991 - June 1996, ¶ 31,036 (00-568 Pet. App. D); Order No. 888-A, 3 F.E.R.C. Stats. ¶ Regs., & 31,048 (00-568 Pet. App. E); Order No. 888-B, 81 F.E.R.C. ¶ 61,248 (00-568 Pet. App. F).

whole national industry in [the] experiment." *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 530 (1945) ("*CL&P*").

SUMMARY OF ARGUMENT

Retail unbundling by a State does not cause any change in the jurisdictional division of regulatory authority under the Federal Power Act. The line between federal and state jurisdiction of transmission remains exactly where it has always been, both under the Act and previously under this Court's constitutional cases that Congress adopted in the statutory law. That line is between wholesale and retail service. It remains for Congress to decide whether to confer on FERC the power over retail transmission that FERC has claimed without statutory warrant.

Under the *Attleboro* line of cases, the States regulated 100% of retail electric service, including 100% of retail transmission. As this Court has said time and again, Congress specifically intended Part II of the Federal Power Act to adopt the *Attleboro* line, and thereby to reserve to the States exclusively all regulatory jurisdiction they had under the *Attleboro* line. Consistent with that congressional intent, the States continued for another 60 years to regulate 100% of retail service, including 100% of retail transmission, under the jurisdictional provisions of the Federal Power Act that remain in effect today. FERC's claim that state decisions to unbundle retail service cause "jurisdictional lines" to "change," with FERC acquiring and the States losing jurisdiction of retail transmission, flouts the congressional intent.

The statutory division between state and federal jurisdiction is between retail and wholesale service. That is a legal standard binding on FERC. That legal standard is not a "question of fact," and may not be evaded in the guise of FERC exercising its fact-finding authority. As this Court's precedent establishes, FERC's fact-finding authority is to determine how an electric utility in fact uses particular transmission facilities — whether to provide retail service, wholesale service or both. The authority to determine whether a facility is used for wholesale transactions in interstate commerce is not authority to change the wholesale/

retail line that marks the statutory limit of FERC's jurisdiction. The statutory line is also not changed by the cases relied upon by the court below, wholesale cases that establish the expansive nature of transmission in interstate commerce but have nothing to do with retail service.

Far from giving FERC "unqualified" jurisdiction of transmission in interstate commerce, the Federal Power Act explicitly qualifies that jurisdictional grant. On the face of the statute, FERC's jurisdiction does not extend to the part of transmission in interstate commerce that constitutes local distribution. On the face of the *Attleboro* case law that Congress adopted, local distribution is retail service.

A leading case in the *Attleboro* line held — and *Attleboro* itself reiterated — that (a) transmission in interstate commerce may extend all the way to the retail customer, and (b) States properly regulate the retail "part" of that transmission in interstate commerce. Congress incorporated this law into the Federal Power Act, not only in the general sense of adopting the *Attleboro* line, but also in the specific sense of adopting the specific case that upheld the States' regulatory jurisdiction over the retail part of transmission in interstate commerce. The same points are also confirmed by this Court's leading precedent on the "local distribution" provision of the Act.

The *Attleboro* line of cases further held that the States properly regulated all — 100% of — service to retail customers, including specifically the utility's delivery of the energy to the retail customer. To describe this state-jurisdictional retail service, case law in the *Attleboro* line used the same "local distribution" term that Congress then used in the Act's jurisdictional section to limit FERC's authority. Congress further provided a statutory rule of construction for the Act's jurisdictional provisions, erroneously ignored by FERC and the court below, that resolves jurisdictional uncertainties in favor of upholding state jurisdiction over matters the States regulated under the *Attleboro* line.

FERC's erroneous claim of jurisdiction over retail transmission is an enormous intrusion into the States' regulatory

authority. It strips from retail customers the protections of public utility regulation for this part of the retail service. In a related context, this Court recently reaffirmed that the States have vital interests in regulating essential public utility service in order to protect retail customers, and that Congress has never limited the States' ability to provide that protection. California's unhappy experience, as well as recent case law involving Order 888, confirm the wisdom of those judgments.

ARGUMENT

I. FERC's Claim Of Jurisdiction Over Retail Transmission Is Contrary to the Purpose of the Federal Power Act, its Legislative History, the Statutory Language and this Court's Decisions.

A. The States Have Always Had Jurisdiction Over Retail Transmission, Because the Purpose of the Federal Power Act Is to Preserve State Jurisdiction.

Congress enacted Part II of the Federal Power Act in 1935. As this Court has said many times, the purpose of that legislation was to "fill" the so-called "*Attleboro* gap" created by *Public Utils. Comm'n of R.I. v. Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927), and its predecessors. *See Arkansas Elec. Coop. Corp. v. Arkansas Public Serv. Comm'n*, 461 U.S. 375, 377-80 (1983) (reviewing cases). The *Attleboro* line of cases had held the States could not constitutionally regulate rates for wholesale transactions in gas and electricity in interstate commerce, while confirming that States could regulate all aspects of retail service. *See, e.g., Missouri v. Kansas Gas Co.*, 265 U.S. 298, 308-309 (1924). The 1935 Act therefore provided for the Federal Power Commission ("FPC") (now FERC) to regulate those wholesale transactions that the States could not. "The premise was that constitutional limitations upon state regulatory power made federal regulation essential if major aspects of interstate transmission and sale were not to go unregulated." *FPC v. Southern California Edison Co.*, 376 U.S. 205, 213 (1964).

In enacting Part II of the Federal Power Act, Congress did not purport to exercise all of the authority it might have exercised

under the Commerce Clause, because its intention was to preserve, not override, state regulatory jurisdiction. *CL&P*, 324 U.S. at 525-27, 529-30. To implement this intent, the "limitations established on [federal commission] jurisdiction . . . were designed to coordinate precisely with those [the *Attleboro* line] constitutionally imposed on the states." *United States v. Public Utils. Comm'n of California*, 345 U.S. 295, 311 (1953) ("*U.S. v. CPUC*"). The result is that the state and federal regulatory commission each has authority on its allocated side of "a bright line easily ascertained, between state and federal jurisdiction." *Southern California Edison*, 376 U.S. at 215.[3]

Consistent with the legislative purpose and "bright line" design, the States continued after the 1935 Act to exercise exclusive regulatory jurisdiction over *all* public utility electric service to retail customers. This included *all* transmission service to retail customers, and *all* facilities used to provide that service. This was so regardless of any physical factors (such as the voltage of lines used for retail service), and regardless of how the facility would now be classified under a "seven-factor" test

---

3. The intent of Congress to preserve and protect the States' regulatory authority within the area delimited by the *Attleboro* line, and to confine federal jurisdiction to the area forbidden to the States, pervades the legislative history. *See, e.g.*, H.R. Rep. No. 74-1318, at 8, 27 (1935) (hereafter, "1935 House Report"); S. Rep. No. 74-621, at 18, 48 (1935) (hereafter, "1935 Senate Report"); *To Provide for Control in the Public Interest of Public Utility Holding Companies Using the Mails and the Facilities of Interstate Commerce, to Regulate the Transmission and Sale of Electric Energy and Natural Gas in Interstate and Foreign Commerce, and for Other Purposes: Hearings on H.R. 5423 Before the House Comm. On Interstate and Foreign Commerce*, 74th Cong. 386, 495, 498, 501, 514, 522-23 (1935) (hereafter, "1935 House Hearings"); *To Provide for the Control and Elimination of Public Utility Holding Companies Operating, or Marketing Securities, in Interstate and Foreign Commerce and through the Mails, to Regulate the Transmission and Sale of Electric Energy in Interstate Commerce, to Amend the Federal Water Power Act, and for Other Purposes: Hearings on S. 1725 Before the Senate Comm. On Interstate Commerce*, 74th Cong. 247, 249-50, 800-01 (1935) (hereafter, "1935 Senate Hearings").

FERC first developed in the order now under review. Pet. App. D19-D20, D124-D125. States exercised their retail delivery jurisdiction regardless of whether the utility was transmitting power from its own generating plant to the retail customer (a plant that could be located either inside or outside of the utility's retail service area), or instead was transmitting to that customer, from a point of interconnection with another electric utility or other generation source, wholesale power the retail utility had purchased.[4]

Congress has never moved its "bright line" between state (retail) and federal (wholesale in interstate commerce) jurisdiction. FERC now says, however, that if a State chooses to unbundle retail power from retail delivery, thus giving retail customers a choice with respect to the identity of their power supplier, it causes a major shift in the jurisdictional line with respect to the delivery. According to FERC, the State loses, and FERC gains, regulatory jurisdiction over an enormous part of the delivery facilities and service to those retail customers — everything that is classified as retail "transmission" rather than

4. As used here, "retail utility" means the electric utility whose facilities (wires) are directly connected to the retail customer's premises. This is the utility that provided all of the electric service to that retail customer before unbundling; and that after unbundling continues to provide at least the retail delivery (transmission) part of the service. "Retail customer" means a person or entity who buys electric power for end use (*i.e.*, does not resell it). "Retail transmission" and "retail delivery" (terms used interchangeably) mean the utility's use of its own transmission and other facilities to deliver electric power to the retail customer at the place of end use.

Of course, many electric utilities provide both retail and wholesale service. In those circumstances, "retail utility" just means that utility to the extent it is providing service to retail customers, and retail transmission (delivery) means the extent to which it is using its own transmission and other facilities to serve retail customers. Where a utility uses a facility (*e.g.*, a transmission line) for both wholesale and retail service, FERC and the state commission each regulates the service within its jurisdiction. This has always been the regulatory scheme under the 1935 Act. *See* p. 19 & n.11, *infra*.

"distribution" under FERC's new seven-factor test. Pet. App. D19-D20, D42, D51-D52.

FERC does not attempt to reconcile this purported surrender of state jurisdiction with the Federal Power Act's basic purpose to preserve state jurisdiction, and to provide federal regulation only where the *Attleboro* line prevented the States from regulating. FERC does not suggest that any pre-Act or post-Act decision of this Court held the States were disabled from exercising any retail transmission jurisdiction. FERC does not deny that the States have continued to exercise this jurisdiction for 60 years under the provisions of the Act that are still in force today. The reasons FERC does give for its jurisdictional claim are deeply flawed, as discussed below.

B. The Case Law and the Legislative History Dispositively Establish That "Local Distribution" Is a "Part" of Transmission in Interstate Commerce That Section 201 Withholds From FERC's Jurisdiction.

The jurisdictional issue arises under Section 201(b)(1) of the Federal Power Act, which provides that the pertinent part of FERC's jurisdiction:

> [S]hall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but . . . shall not apply to any other sale of electric energy . . . . [FERC] shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce . . . .

16 U.S.C. § 824(b)(1).

That statutory language is the primary reason FERC gives why "jurisdictional lines change" when States unbundle retail service. According to FERC:

> [W]e find compelling the fact that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.

Pet. App. D43, E29. FERC's statement is wrong. Section 201 does not give FERC "unqualified" jurisdiction over transmission in interstate commerce

FERC's "without qualification" contention assumes that "local distribution" under Section 201 is, somehow, *not* transmission in interstate commerce. In fact, both the case law leading up to the Federal Power Act and the Congress that enacted it understood that interstate energy moves in a continuum from source to end use.[5] In appreciation of that technological reality, Congress prohibited federal control over the part of the continuum in interstate commerce that the *Attleboro* line put within the States' regulatory ambit.

As shown by the *Attleboro* line of cases, by the legislative history, and by this Court's leading post-Act decision, local distribution is one part — a subset — of transmission in interstate commerce. It also is a part that Section 201 "on its face" *withholds* from FERC's jurisdiction. Because that is so, FERC's logic collapses. Bundled or unbundled makes no difference. Either way, the statute preserves state jurisdiction over the local distribution part of transmission in interstate commerce — which means retail transmission in interstate commerce.

A leading case in the *Attleboro* line involved a retail gas utility that (1) transported gas from Pennsylvania to New York, and (2) sold the gas to retail customers in New York.

5. Pre-Act cases cited to Congress were particularly sophisticated about electricity, including the instantaneous nature of generation, transmission and use. *See Utah Power & Light Co. v. Pfost*, 286 U.S. 165, 177-81 (1932) (discussed in the 1935 Senate Report at 48, 1935 Senate Hearings at 801-02, and 1935 House Hearings at 97); *South Carolina Power Co. v. South Carolina Tax Comm'n*, 52 F.2d 515, 523-24 (E.D. S.C. 1931), *aff'd mem.*, 286 U.S. 525 (1932) (cited in the 1935 Senate Hearings at 802).

Pennsylvania Gas Co. v. Public Service Comm'n, 252 U.S. 23, 27-28 (1920). This Court was quite clear on three points that refute FERC's jurisdictional theory. First, all of the movement of the gas — from source all the way to the retail customer — was transmission in interstate commerce:

> [T]he gas is transmitted directly from the source of supply in Pennsylvania to consumers in the cities and towns of New York .... The transmission is continuous and single and is, in our opinion, a transmission in interstate commerce ....

252 U.S. at 28. Second, New York, in regulating the gas service to retail customers, was regulating a "*part*" of the transmission in interstate commerce:

> The thing which the State Commission has undertaken to regulate, while *part of an interstate transmission*, is local in nature, and pertains to the furnishing of natural gas to local consumers ....

Id. at 30-31 (emphasis added).

Third, although this retail service ("furnishing of natural gas to local consumers") was part of the transmission in interstate commerce, the State was *permitted* to regulate it:

> While the manner in which the business is conducted is part of interstate commerce, its regulation in the distribution of gas to local consumers is required in the public interest and has not been attempted under the superior authority of Congress.

Id. at 31. These points were reiterated in *Attleboro* itself, including that the state commission in *Pennsylvania Gas* permissibly regulated "part of an interstate transmission" in regulating retail service. 273 U.S. at 87-88.

The legislative history of the 1935 Act establishes, beyond a shadow of a doubt, that Congress knew about and specifically intended to adopt *Pennsylvania Gas*. This express legislative adoption of *Pennsylvania Gas* is stated in the 1935 Senate Report at 48. It is stated in a legal Memorandum authored by the FPC's

General Counsel and its Solicitor.[6] 1935 Senate Hearings at 800-01. The adoption of *Pennsylvania Gas* is substantively stated in a section-by-section analysis FPC Commissioner Seavey gave the House Committee and FPC Solicitor DeVane gave the Senate Committee (saying that "even where the energy comes directly from another State," state jurisdiction "is expressly preserved"). 1935 House Hearings at 386; 1935 Senate Hearings at 247. It is explained by Solicitor DeVane in the 1935 Senate Hearings at 250, and in the 1935 House Hearings at 498, 518, 521-22.

In writing *Pennsylvania Gas* into the Federal Power Act, Congress adopted its holdings that (1) transmission of energy may be transmission in interstate commerce all the way to the retail customer; (2) regulation of retail service is regulation of a "part" of transmission in interstate commerce; and (3) the States properly exercise regulatory jurisdiction over this retail "part." Indeed, these specific aspects of *Pennsylvania Gas* were pointed out to the congressional committees. 1935 House Hearings at 521-22; 1935 Senate Hearings at 761. In testifying that the FPC's bill adopted *Pennsylvania Gas*, the FPC's Solicitor DeVane stated the consequences for federal jurisdiction:

> This bill does *not* give the Commission jurisdiction over energy that is *transmitted in interstate*

6. As this Court has observed, the original 1935 bill (the portions that added to the Federal Power Act) was prepared by the FPC itself. *CL&P*, 324 U.S. at 525, 529. The FPC's bill was presented to Congress by FPC Commissioner Seavy and the FPC's Solicitor DeVane, both of whom had participated in its preparation. 1935 House Hearings at 384, 400-01, 449-50, 515, 553.

This Court has extensively used the legislative history to interpret the jurisdictional scope of the 1935 Act, *e.g.*, *Southern California Edison*, 376 U.S. at 213 & n.8; *CL&P*, 324 U.S. at 525-27 & nn.2-5; *Jersey Central Power & Light Co. v. FPC*, 319 U.S. 61, 68 n.7, 71 & n.10, 76-77 & nn.21-24 (1943), and similarly has used the counterpart legislative history of the Natural Gas Act to construe its comparable jurisdictional provisions, *e.g.*, *Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n of Indiana*, 332 U.S. 507, 515 n.11, 517-19 nn.13-14 (1947).

> *commerce by a particular company and sold by that company to consumers*.

1935 Senate Hearings at 250 (emphasis added).

This Court confirmed these points in what FERC admits is the leading case interpreting the "local distribution" limitation on its jurisdiction under Section 201. In *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515 (1945) ("*CL&P*"), this Court was clear that, when any part of the electricity moves across state lines, transmission all the way to the retail customer is transmission in interstate commerce.

> Technology of the business is such that if any part of a supply of electric energy comes from outside of a state it is, or may be, present in every connected distribution facility. *Every facility from generator to the appliance for consumption may thus be called one for transmitting such interstate power. By this test the cord from a light plug to a toaster on the breakfast table is a facility for transmission of interstate energy if any part of the load is generated without the state*. It has never been questioned that technologically generation, transmission, distribution and consumption are so fused and interdependent that the whole enterprise is within the reach of the commerce power of Congress, either on the basis that it is, or that it affects, interstate commerce, if at any point it crosses a state line.

324 U.S. at 529-530 (emphasis added).

The Court was equally clear that, notwithstanding this technologically expansive scope of transmission in interstate commerce, the 1935 Act was not intended to take from the States (or even "disturb") their jurisdiction under the *Attleboro* line. *Id.* at 525-27. Specifically, this limitation on federal jurisdiction is embodied in Section 201's "local distribution" provision. *Id.* at 530-31.

> The assurance which the sponsors of this legislation expressed as to protection of the general jurisdiction of a state over electric utilities of this character . . . is to be found in the words of § 201(b), "but shall not have jurisdiction, except as provided in this Part and the Part next following, . . . over facilities used in local distribution . . . ."

Id. at 527. Accordingly, it is irrelevant that interstate energy is transmitted in local distribution facilities:

> It does not seem important whether out-of-state energy gets into local distribution facilities. They may carry no energy except out-of-state energy and still be exempt under the Act. The test is whether they are local distribution facilities.

Id. at 531.

Therefore, this Court held, *it is not sufficient for federal jurisdiction that a facility is used for "transmission in interstate commerce."* Rather, it *is also* necessary that the facility is *not* used for "local distribution":

> The order [asserting FPC jurisdiction] must stand or fall on whether this company owned facilities that *were* used in transmission of interstate power *and which were not facilities used in local distribution.*

Id. (emphasis added).

For these reasons, *CL&P* vacated the FPC's order. The agency had "found that each of the facilities in question is 'used for the transmission of electric energy purchased as aforesaid from the Connecticut Power Company, as distinguished from local distribution thereof.'" *Id.* at 532. That did not establish federal jurisdiction because:

> [The FPC] *has not, however, made an explicit finding that these facilities are not used in local distribution*; and we are in doubt whether by application of the statute as herein construed it could have done so . . . Nothing except explicit findings excluding the grounds of state control gives assurance that the

> bounds of federal jurisdiction have been accurately understood and fully respected . . . .

Id. at 532 (emphasis added).

Thus, under this Court's controlling precedent, as well as the pre-Act case law incorporated into the Act and the legislative history, FERC is wrong in asserting it has jurisdiction over transmission in interstate commerce "without qualification." Some transmission in interstate commerce is also local distribution. Congress gave FERC jurisdiction only over the part of that transmission which is not associated with delivery to retail customers.

C. The Case Law and the Legislative History Dispositively Establish That "Local Distribution" Under Section 201 Includes Retail Transmission.

A second step in FERC's legal argument builds on the first, and claims the meaning of "local distribution" is not clear. According to FERC, the "relevant legislative history . . . does not directly address the issue of what constitutes local distribution as opposed to transmission in interstate commerce." Pet. App. D96. As discussed, local distribution and transmission in interstate commerce are not mutually exclusive categories. Furthermore, the "relevant legislative history" — and the case law — could not be clearer on the meaning of "local distribution."

Again, the purpose of the 1935 Act was to fill the *Attleboro* gap while not taking any regulatory authority from the States. *CL&P*, 324 U.S. at 526. Therefore — no surprise — in the legislation "Congress . . . adopted the 'mechanical' line established in *Kansas Gas* and *Attleboro* as the statutory line dividing federal and state jurisdiction." *Arkansas Elec. Coop.*, 461 U.S. at 380. By using the *Attleboro* line, "Congress . . . was meticulous to take in only territory which this Court had held the states could not reach." *Panhandle Eastern Pipe Line Co. v. Michigan Public Serv. Comm'n*, 341 U.S. 329, 335 (1951) ("*Panhandle/Michigan*"), quoting *Panhandle Pipe Line Co. v.*

Public Serv. Comm'n of Indiana, 332 U.S. 507, 519 (1947) ("*Panhandle/Indiana*"). The Court has said this time and again.[7]

The *Attleboro* line's division between state and federal jurisdiction is equally clear. *Attleboro* itself applied to electricity the jurisdictional line used for natural gas in *Missouri v. Kansas Gas Co.*, 265 U.S. 298 (1924). *See Attleboro,* 273 U.S. at 88-89; *see also Arkansas Elec. Coop.*, 461 U.S. at 378 ("the wholesale/retail line drawn in . . . *Kansas Gas*"); *Southern California Edison*, 376 U.S. at 212 (*Attleboro* "held that *Kansas Gas* . . . controlled").

In turn, *Kansas Gas* held that state regulatory jurisdiction began once out-of-state gas was delivered to an in-state retail utility (called a "distributing company"). 265 U.S. at 308. Behind that line, the State had *complete* regulatory jurisdiction of *all* of the retail utility's service to retail customers. This included not only sale of the gas but also its delivery to the retail customer:

> [The] subsequent sale *and delivery* by these companies to their customers *at retail* is intrastate business and subject to State regulation.

Id. (emphasis added).

Thus, the line between state and federal jurisdiction, drawn by *Attleboro* and its predecessors, is located where electricity in interstate commerce is received by in-state retail utilities. That line, which is precisely the one Congress drew with the local distribution provision in the 1935 Act, puts *all of the retail service* on the States' side — which means that all of the utility's retail facilities and operations, including retail transmission, are subject to state jurisdiction.

---

7. *Southern California Edison*, 376 U.S. at 214 ("What Congress did was to adopt the test developed in the *Attleboro* line"); *U.S. v. CPUC*, 345 U.S. at 311 ("Part II is a direct result of *Attleboro*. They are to be read together"); *Panhandle/Indiana*, 332 U.S. at 518 ("The basic purpose of the present legislation is to occupy this field in which the Supreme Court has held that the States may not act") (quoting legislative history). Cases decided under the Natural Gas Act are direct authority on this jurisdictional issue under the Federal Power Act. *Southern California Edison*, 376 U.S. at 211-15; *U.S. v. CPUC*, 345 U.S. at 311.

Kansas Gas involved a common fact pattern, where the utility that transmits energy into a State sells it at wholesale to a local utility that provides retail service. As discussed above, *Pennsylvania Gas* addressed a different situation, where the same company doing the interstate transmission also provides retail service to consumers in the importing State. In that situation as well, this Court upheld the State's authority to regulate the retail service. 252 U.S. at 29-31. *See also U.S. v. CPUC*, 345 U.S. at 303 ("*Attleboro* reiterated and accepted the holding of *Pennsylvania Gas* . . . that sales across the state line direct to consumers is a local matter within the authority of . . . the importing state"). As noted, in accordance with the assurance that the 1935 Act would not take from the States any regulatory jurisdiction they had under the *Attleboro* line, the legislative history repeatedly affirms that the Act would not change the result in the *Pennsylvania Gas* situation either.[8]

Standing alone, the above points would establish unquestionably that local distribution facilities under Section 201 include all retail transmission facilities. States regulated all retail service, including all retail delivery, under the *Attleboro* line. Congress promised to adopt the *Attleboro* line so that all state authority would be preserved. Congress kept its promise by "forbid[ding]" federal jurisdiction over local distribution facilities in Section 201. *CL&P*, 324 U.S. at 528-31.

But the above points do not stand alone. *Kansas Gas*, the very case that *Attleboro* followed, used the term "local distribution" to encapsulate the retail service, including delivery, that was subject to state regulation — both when provided by an in-state retail utility, and also when provided by the utility that transmitted the energy across state lines.

> The business of supplying, on demand, local consumers is a local business, even though the gas

---

8. *E.g.*, 1935 Senate Report at 48; 1935 Senate Hearings at 250 (FPC Solicitor DeVane), 800-01 (legal Memorandum prepared by FPC attorneys). Indeed, the FPC's Solicitor said regarding *Pennsylvania Gas* that "we are writing the Supreme Court's decisions in this bill." 1935 House Hearings at 523; *see id.* at 498, 499, 518, 521-22.

> be brought from another State and drawn for distribution directly from interstate mains; and this is so whether the *local distribution* be made by the transporting company or by independent distributing companies.

265 U.S. at 309 (emphasis added).

Thus, transmission (delivery) service to retail customers was not only state-jurisdictional under the *Attleboro* line, it was also called "local distribution." *See also Arkansas Elec. Coop.*, 461 U.S. at 377-78. As if to hammer the last nail home, the legislative history says that facilities for local distribution include "transmission lines":

> Insofar as the facilities are concerned, [the bill] takes no jurisdiction away from the States, but it does confer additional jurisdiction upon this Commission as to those facilities that have to do with interstate transmission.
>
> I want to make that distinction very clear, because it has nothing to do with facilities that relate only to local distribution *or to transmission lines used for local distribution.*

1935 House Hearings at 501 (FPC Solicitor DeVane) (emphasis added).

FERC did not confront this dispositive case law and legislative history. Instead, it claimed its jurisdictional theory is supported by statements in the Senate Report that Section 201 was amended to clarify that FERC's jurisdiction "includes interstate transmission where there is no sale"; and that federal jurisdiction "is asserted . . . over all interstate transmission lines whether or not there is a sale of the energy carried." Pet. App. at D97-D98 (quoting 1935 Senate Report at 19, 48). In fact, these references to federal jurisdiction where there is "no sale" relate to Congress's adoption of *Pennsylvania Gas*, under which States have regulatory jurisdiction over retail service where the retail utility's operations extend across state lines.

In the *Pennsylvania Gas* situation, it was often difficult for a State to regulate the retail service effectively, because the state commission did not have jurisdiction over and was unable to obtain information about the true cost of the utility's facilities located out-of-state but used to provide in-state retail service. 1935 Senate Hearings at 247. For this reason, the 1935 Act empowered the FPC to *assist* state commissions by investigating and determining the cost of out-of-state facilities — *i.e.*, to "aid the State commissions in determining just and reasonable rates for energy by companies having properties in more than one State." *Id.*; 1935 House Hearings at 385; *see also* 1935 House Report at 8; 1935 House Hearings at 519-20. This federal assisting power is still found today in 16 U.S.C. § 824e(d), which gives FERC authority to investigate and determine costs "in cases where [it] has no authority to establish a rate governing the sale of such energy."[9]

Congress clearly intended to (and did) give the FPC assisting jurisdiction where there is "no sale." To have this assisting power, the FPC had to be given jurisdiction of "interstate transmission where there is no sale" — *i.e.*, jurisdiction over the out-of-state facilities whose cost the federal commission is to determine for the state commission. *See id.* But this limited assisting authority is a far cry from the regulatory authority FERC claims to set rates, terms and standards for, and otherwise control, retail transmission service.[10]

9. The references in the Senate Report to federal jurisdiction over facilities "where there is no sale" and "whether or not there is sale of the energy" mean jurisdiction regardless of whether there is a sale at *wholesale* (the absence of which being the reason why FERC would have "no authority to establish a rate," 16 U.S.C. § 824e(d)). *See* 1935 Senate Hearings at 247 (FPC's section-by-section analysis) ("where no wholesale rate is involved"); 1935 House Hearings at 385 (same). If there truly is "no sale" of any kind, FERC has no jurisdiction because Section 201 excludes facilities for transmission of energy "consumed wholly by the transmitter." 16 U.S.C. § 824(b)(1).

10. In addition to the FPC's assisting power, the Senate Report's statement about federal jurisdiction over interstate transmission facilities (Cont'd)

D. The Scope of FERC's Jurisdiction is Established by Statute and is not a Factual Inquiry.

In *CL&P*, this Court made plain that, because "technologically" every facility from the generator to the retail customer (including the customer's "cord from a light plug to a toaster on the breakfast table") is a "facility for transmission of interstate energy," Congress intentionally chose not to legislate to the full extent of its power under Commerce Clause. 324 U.S. at 529-30. Instead, Congress' "constant purpose [was] to protect" state authority under the *Attleboro* line. *Id.* at 525-26. Because Congress effectuated this purpose by prohibiting federal jurisdiction "over facilities used in local distribution," *id.* at 527, 530-31, this Court held the local distribution "phrase to be a limitation on jurisdiction and a legal standard that must be given effect in this case in addition to the technological transmission test," *id.* at 531.

To support its claim that a State's unbundling of retail service causes the Act's "jurisdictional lines" to "change," FERC invoked this Court's statement reaffirming *CL&P* and adding that the federal agency is to decide fact issues:

> Whether facilities are used in local distribution — although a limitation on FPC jurisdiction and a legal standard that must be given effect in addition to the technological transmission test . . . — involves a question of fact to be decided by the FPC as an original matter.

Pet. App. D112 (quoting *Southern California Edison*, 376 U.S. at 210 n.6). Based on this quotation, FERC says that it "cannot

(Cont'd)
"whether or not there is sale of the energy carried" may also refer to interconnection authority under Section 202 (16 U.S.C § 824a(b)-(d)), or even to a broader concept of FPC "coordination" authority. 1935 Senate Report at 48. The Senate bill would have given the FPC jurisdiction over generation as well as transmission facilities, saying that the "physical inseparability of generation and transmission . . . makes regulation of transmission impossible unless generation is also controlled." *Id.* at 48-49. The House excluded generation facilities from FPC jurisdiction, however. 1935 House Report at 27; *see* 16 U.S.C. § 824(b)(1).

divine" a "bright [jurisdictional] line for unbundled retail transmission by the public utility that previously provided bundled retail service"; and that "whether facilities are used in local distribution" after retail unbundling "is a question of fact to be decided by the Commission as an original matter." Pet. App. D48 & n.546. *See also, e.g., id.* at D123, E31 & n.453 (finding itself "particularly persuaded" by this argument), E46.

Contrary to FERC's argument, the *Southern California Edison* footnote shows on its face that the "question of fact" to be decided by FERC "as an original matter" is how any particular facility is *used* by the utility — *i.e.*, for retail service, wholesale service, or both. 376 U.S. at 210 n.6. In that case, the FPC found (and this Court found evidence to support) that some of the utility's facilities were used — indeed, were used exclusively — to *sell wholesale power to another utility*. Those facilities included both a substation and portions of two 12 kv. lines that extended beyond the point where the utility's last retail customer was served. *Id.*[11]

This FERC fact-finding authority — to determine the manner in which a given transmission facility of a given utility is used, and specifically to determine whether it is used to supply the "interstate commerce" element for FERC-jurisdictional wholesale transactions — does not empower the agency to circumvent the local distribution "*legal standard* that must be given effect in addition to the technological transmission test . . . ." *Id.* (emphasis added); *CL&P*, 324 U.S. at 531-32. *Cf. Allentown Mack Sales and Serv., Inc. v. NLRB*, 522 U.S.

11. A given facility (such as a transmission line) may be used by a utility to provide electric service to both retail and wholesale customers, but such "dual use" has not created significant jurisdictional problems under the Federal Power Act. The state and federal regulator each regulates the service within its jurisdiction. As FERC said in Order 888-A, for example, costs of dual use facilities are allocated between the federal (wholesale) and state (retail) jurisdiction for ratemaking purposes. 3 F.E.R.C. Stats. & Regs., ¶ 31,048, at 30,414 & n.707. The same point is discussed in the legislative history. 1935 House Hearings at 505 (FPC Solicitor DeVane).

359, 376 (1998) ("An agency should not be able to impede judicial review, and indeed even political oversight, by disguising its policymaking as factfinding"). Under the local distribution legal standard, where a State chooses to unbundle retail service, the Federal Power Act's line between state and federal jurisdiction shines as brightly in the same location as ever: All electric service by a retail utility to a retail customer, including specifically transmission service for that customer, is on the State's side of the line. FERC's need to decide fact issues about whether particular facilities are used for wholesale service in interstate commerce is no basis for the agency to blind itself or others to the bright line legal standard that Congress adopted.

Based on its faulty premise that local distribution is only a "question of fact," FERC announced its seven-factor test for divvying up retail "transmission" and "local distribution" facilities (and taking jurisdiction over everything that falls into the retail "transmission" category). Pet. App. D123-D125. *FERC* did not purport to show that its test for local distribution facilities has *any* connection with Congress' reason for that statutory provision — which was to preserve state regulatory jurisdiction. To the contrary, the seven-factor test is designed to shift retail transmission jurisdiction to FERC, thereby serving its proclaimed interests "in preventing any balkanization of the interstate power market," Pet. App. D46, and "ensur[ing] that non-discriminatory transmission services are provided to all potential retail power competitors," *id.* at E48.

However, the States are free under the Federal Power Act to maintain so-called "balkanization" and "discrimination" in the retail power market, by retaining the traditional system of monopoly utility service and regulation for retail power. Congress has forbidden FERC from circumventing that State decision. 16 U.S.C. § 824k(g)-(h). FERC's interests in the retail market are unexplained.[12]

12. As this Court recognized, Congress may have intended precisely to preserve "balkanization" in service to other, fundamental values:

(Cont'd)

Particularly damning is FERC's admission that its seven-factor test may result in the conclusion that *no* local distribution facilities are used for retail service in a given situation. Pet. App. D48-D49. That FERC's test can eliminate any "local distribution facility" for retail service — the statutory category intended by Congress to preserve state jurisdiction, under a statutory provision "the Commission must observe and the courts must enforce," *CL&P*, 324 U.S. at 529 — demonstrates fundamental error frustrating the will of Congress.

Finally, FERC's seven-factor test blatantly does what none of the regulatory cases in the *Attleboro* line ever did, and none of this Court's cases under the Federal Power Act has ever done. FERC's test goes behind the point of delivery of interstate power to the retail utility and, based on factors like voltage, splits the utility's retail facilities and operations into Federal and State

(Cont'd)

> [S]tate lines and boundaries cut across and subdivide what scientifically or economically viewed may be a single enterprise. Congress is acutely aware of the existence and vitality of these state governments. It sometimes is moved to respect state rights and local institutions even when some degree of efficiency of a federal plan is thereby sacrificed. Congress may think it expedient to avoid clashes between state and federal officials in administering an act such as we have here. Conflicts which lead state officials to stand shoulder to shoulder with private corporations making common cause of resistance to federal authority may be though to be prejudicial to the ends sought by an act and regulation more likely to be successful, even though more limited, if it has local support. Congress may think complete centralization of control of the electric industry likely to overtax administrative capacity of a federal commission. It may, too, think it wise to keep the hand of state regulatory bodies in this business, for the "insulated chambers of the states" are still laboratories where many lessons in regulation may be learned by trial and error on a small scale without involving a whole national industry in every experiment.

CL&P, 324 at 530.

regulatory camps. This cannot be reconciled with the statute Congress enacted, which "adopted the 'mechanical' line established in *Kansas Gas* and *Attleboro* as the statutory line dividing federal and state jurisdiction." *Arkansas Elec. Coop.*, 461 U.S. at 380. Under that *statutory* line:

> With the delivery of the gas to the distributing companies . . . the interstate movement ends. Its subsequent sale and delivery by these companies to their customers at retail is intrastate business and subject to state regulation.

Kansas Gas, 265 U.S. at 308.[13]

E. FERC's Jurisdictional Analysis Misuses This Court's Precedents.

As support for the "changing jurisdiction lines" theory, FERC places much emphasis, and the court below placed exclusive emphasis, on *FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972), and *Jersey Central Power & Light Co. v. FPC*, 319 U.S. 61 (1943). These cases could not be more inapposite. Each shows, on a particular fact pattern involving wholesale transactions, the expansive nature of "transmission in interstate commerce" when electric systems are interconnected (which simply illustrates *CL&P*'s point about "the [t]echnology of the business," 324 U.S. at 529).[14]

In contrast, this case concerns a public utility's use of its own wires to provide service to its retail customers, and whether

13. The fate of the one decision of this Court that jurisdictionally divided an in-state utility's retail facilities and operations under the Natural Gas Act, *FPC v. East Ohio Gas Co.*, 338 U.S. 464 (1950), is addressed below.

14. The *Jersey Central* opinion states that the utility was selling power to another utility (*i.e.*, selling at wholesale). 319 U.S. at 64-65, 68. The *Florida Power* opinion states that the utility exchanged power with four other utilities, 404 U.S. at 456 & n.4, which is also a type of wholesale transaction, *see id.* at 458. This is elaborated by the portion of the FPC hearing officer's opinion the Court discussed (*id.* at 456 n.4). *See Florida Power & Light Co.*, 37 FPC 544, 1966 FPC LEXIS 427, *4-6 (July 12, 1966); *see also id.* at *1.

that use is for the local distribution that is exempted from FERC's jurisdiction over transmission in interstate commerce. Neither *Florida Power* or *Jersey Central* has the slightest thing to do with retail service, retail customers, retail transmission or local distribution facilities. They are no support at all for FERC's position on the issue presented here.

In fact, *Florida Power* undermines FERC's position. The Court reiterated that Part II of the 1935 Act "fills the 'Attleboro gap,'" and therefore applies to exchanges of power between utilities across state lines. 404 U.S. at 458. The Court also rejected the utility's argument that reserved state jurisdiction needed more protection than "the 'engineering and scientific test' that controls this case" — *i.e.*, a case involving *wholesale* transactions. *Id.* at 467. In doing so, the Court reiterated that Section 201(b)'s local distribution provision protects the jurisdiction the Act reserves to the States:

> On top of the "engineering and scientific test" that controls this case, the Federal Power Act imposes a "legalistic or governmental" test. Federal jurisdiction may not reach "facilities used in local distribution" of energy. 16 U.S.C. § 824(b). Thus, *state jurisdiction is clearly demarcated and preserved. Connecticut Light & Power Co. v. FPC*, 324 U.S. 515 (1945).

Id. (emphasis added).[15]

15. Presumably as support for its seven-factor test, FERC at one point refers to the statement in *U.S. v. CPUC*, 345 U.S. at 316, that "the facilities supplied 'local distribution' only after the current was subdivided for individual consumers." Pet. App. D116. In that case, however, the FPC asserted jurisdiction over *wholesale* transactions. 345 U.S. at 297-98. This Court indicated that wholesale transactions would be exempt from federal jurisdiction if local distribution facilities were used (but said the wholesaler was not using such facilities on the facts presented). *See id.* at 316. *Accord Southern California Edison*, 376 U.S. at 210 & n.6. FERC's attempt to apply wholesale cases out-of-context to retail service is inappropriate. In particular, the concept of a wholesaler "subdividing" electric power (a notion analogous to the

(Cont'd)

For its jurisdictional theory, FERC also put considerable emphasis on *FPC v. East Ohio Gas Co.*, 338 U.S. 465 (1950). Pet. App. D119-D120. That case, decided under the Natural Gas Act, did "split" a utility's retail operations and facilities, and allowed the FPC to assert jurisdiction based on the utility's high pressure pipelines that carried gas to the communities it served at retail. For a variety of reasons, *East Ohio* does not support FERC's position that retail service can become FERC-jurisdictional under the Federal Power Act.

One reason is that, as this Court recently noted, Congress promptly reversed *East Ohio* with legislation that returned in-state retail gas utilities to exclusive state jurisdiction — "*as always has been intended.*" *General Motors Corp. v. Tracy*, 519 U.S. 278, 293 (1997) (emphasis added) (quoting S. Rep. No. 817, 83d Cong., 1st Sess., 1-2 (1953)). The decision was wrong and was decisively repudiated.

Furthermore, *East Ohio* necessarily rejected the jurisdictional analysis in *Pennsylvania Gas*, 252 U.S. 23. *See East Ohio*, 338 U.S. at 470 n.10. After *East Ohio*, however, this Court returned to *Pennsylvania Gas* and its jurisdictional analysis in *Panhandle/Michigan*, 341 U.S. at 333, 337, a decision this Court recently — and forcefully — reaffirmed. *General Motors v. Tracy*, 519 U.S. at 292, 305-06. Thus, *East Ohio's* jurisdictional analysis was also wrong and repudiated.[16]

(Cont'd)
"original package" doctrine employed in tax cases and discussed below) is inapplicable to the local distribution issue in the *retail* service context. This Court has so held. *CL&P*, 324 U.S. at 533-34.

16. In rejecting *Pennsylvania Gas*, the *East Ohio* opinion relied on the reasoning in *East Ohio Gas Co. v. Tax Comm'n*, 283 U.S. 465 (1931). *See* 338 U.S. at 470 n.10, 472-73 n.13. The first *East Ohio* decision was a case involving state taxation, however. If it had adopted the analysis in *Pennsylvania Gas*, which considered the transmission in interstate commerce to extend all the way to the retail customer, the State could not have been allowed to tax in *East Ohio* under the then-standard rule that States could not directly tax interstate commerce.

(Cont'd)

Finally, *East Ohio*, whatever its stature under the Natural Gas Act, could not possibly be correct under the Federal Power Act. As reviewed above, the legislative history states — again and again — that this Act *adopts Pennsylvania Gas*.

II. FERC's Construction Of Section 201 Is Not Entitled to Deference.

In the alternative to relying on *Florida Power* and *Jersey Central*, the court below said FERC's jurisdictional ruling should be affirmed under "the deferential standard" of *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). Pet. App. C33. This is error. The "deference" principle of *Chevron* is, at bottom, a rule of statutory construction. *See* 467 U.S. at 843 n.9. Congress provided for a different rule of construction under the Federal Power Act.

Section 201(a), 16 U.S.C. § 824(a), sets forth a declaration of purpose for the 1935 additions to the Federal Power Act. In what this Court has called the legislation's "policy declaration" and "policy provision," the last phrase of Section 201(a) provides "that federal regulation is 'to extend only to those matters which are not subject to regulation by the States . . . . '" *CL&P*, 324 U.S. at 527. This policy provision does not "nullify a clear and specific grant of jurisdiction," but also "cannot be wholly ignored." *Id.*

(Cont'd)
The first *East Ohio* case avoided that result (and so upheld state authority to tax) by reasoning analogous to the "original package" doctrine used for other commodities. *See* 283 U.S. at 470-71 . This kind of reasoning, which as applied to energy focuses upon factors like "reducing the pressure" and "dividing the energy," was commonly used in taxation cases of that era. *See, e.g., Southern Nat. Gas. Corp. v. Alabama*, 301 U.S. 148, 154-55 (1937). It was not the basis for the *Attleboro* line addressed to state *regulatory* jurisdiction, however, and (as this Court held) is not the proper analysis for determining "local distribution" facilities under the Federal Power Act. *CL&P*, 324 U.S. at 533-34.

> [S]uch a declaration is relevant and entitled to respect as a guide in resolving any ambiguity or definiteness in the specific provisions which purport to carry out its intent.

Id. Therefore, if the meaning of the local distribution provision is "otherwise in doubt[, it] *should be read in harmony with [Section 201(a)'s] policy provision.*" *Id.* at 529 (emphasis added); *see also id.* at 533.

Thus, the statute contains its own rule of construction to be used when the meaning of the jurisdictional provision is uncertain. That rule is to preserve state authority in matters States could regulate under the *Attleboro* line. Retail transmission certainly qualifies as a "matter[] . . . subject to regulation by the States." States have regulated it from Day One under the 1935 Act. Accordingly, any reasonable doubt about FERC's "changing transmission jurisdiction" thesis is resolved against FERC by Section 201(a)'s rule of construction.

Of course, *Chevron* itself does not yield deference to FERC's "changing lines" interpretation of its jurisdiction under Section 201. As the Court said:

> The judiciary . . . must reject administrative constructions which are contrary to clear congressional intent. . . . If a court, employing traditional tools of statutory construction, ascertains that Congress had an intention on the precise question at issue, that intention is the law and must be given effect.

467 U.S. at 843 n.9. Here, Congress *did* have "an intention on the precise question at issue." As this Court has repeatedly said, the intention was to adopt the *Attleboro* line. The legislative history materials — "traditional tools of statutory construction" — establish beyond question that Congress did not intend to take any regulatory jurisdiction from the States. As States always regulated transmission to retail customers, "that is the end of the matter." *Chevron*, 467 U.S. at 842.

III. The Consequences Of FERC's Assertion Of Jurisdiction Over Retail Transmission Are Terribly Intrusive Of State Regulatory Authority.

California's deregulation scheme for retail electricity required the State's large privately-owned utilities to transfer control (though not ownership) of their transmission facilities to an Independent System Operator ("ISO"). The ISO is a state-created, non-profit corporation that operates the ceded transmission as a coordinated system.[17] The state legislation that created the ISO made it subject to supervisory control by a state-created Oversight Board.[18] California and FERC have disagreed, frequently and deeply, about important matters concerning these state-created institutions.

From the outset, FERC claimed authority to negate the Oversight Board's supervisory functions.[19] Recently, FERC has claimed authority to dismiss the ISO's Governing Board and give temporary control of the State's transmission system to management personnel, contrary to California corporation law; to change the constituencies of the Governing Board; and to specify the qualifications for Board members and the manner of their selection — all so as to bypass control of the ISO by the government of the State that created the institution and provided its authority.[20] These controversies have been punctuated by

---

17. Cal. Pub. Util. Code §§ 345 *et seq.*

18. Cal. Pub. Util. Code §§ 335, 348. The statutory findings explain that maintaining the transmission system and reliable electric service are "of paramount importance" to health, safety and economic welfare; and therefore that, in providing for retail deregulation, the Legislature created the Oversight Board to maintain public accountability and ultimate control over the ISO and "various market-based mechanisms." Cal. Pub. Util. Code § 334.

19. *Pacific Gas & Elec. Co.*, 77 FERC ¶ 61,204, at 61,817-19 (1996).

20. *San Diego Gas & Elec. Co. v. Sellers of Energy*, 93 FERC ¶ 61,121, at 61,362-64 (2000) (proposed order), 93 FERC ¶ 61,294, at 62,012-14 (2000) (final order).

threats of FERC lawsuits,[21] and FERC's recent action was described as "needlessly provoking a constitutional showdown."[22] This intrusion deep into state affairs is premised on the erroneous assertion of the shifted jurisdictional line.

The consequences of FERC's jurisdictional thesis run deeper. States exercise jurisdiction over retail transmission, including rates and other terms and conditions of service, in light of the legal duties a public utility owes to its retail customers. These duties, which are imposed by state statutes, regulations and utility franchises, traditionally include obligations to serve all customers in the utility's service area without discrimination, and to provide adequate service. The obligation to provide adequate service includes construction and maintenance of physical facilities (including transmission facilities) sufficient to supply the amount of retail service demanded. There are often special rules to protect essential service to particularly vulnerable members of the community, and allocation rules for times of shortage or emergency. This Court has recently affirmed these deeply engrained local concerns as being of particular importance in utility-related Commerce Clause litigation. *See General Motors v. Tracy*, 519 U.S. at 290 (a public utility's monopoly on essential service is "balanced by regulation and the imposition of obligations to the consuming public"); *id.* at 294-97 (discussing public utility regulations and obligations of retail gas utilities), *id.* at 306 (discussing the States' "important interests" in regulating retail service, including that residential customers "are not frozen out of their houses in the cold months").

In contrast to state-regulated retail service, federal law does not impose these general public utility-type service obligations on the FERC-jurisdictional portion of an electric utility's

21. *California Power Exch. Corp.*, 1998 FERC LEXIS 2361, at *30-31 (Nov. 24, 1998); *San Diego Gas & Elec. Co. v. Sellers of Energy*, 2000 FERC LEXIS 2491, at *207-08 (Dec. 15, 2000) (Hoecker, concurring further) (issued Jan. 18, 2001).

22. *San Diego Gas & Elec.*, 93 FERC ¶ 61,121, at 61,386 (Herbert, concurring).

business. Congress refused the FPC's request for provisions in the 1935 Act that would have created public utility obligations at the federal level and given the federal agency jurisdiction over construction of transmission and other facilities.[23] As a consequence, and as FERC stated in a Notice underlying Order 888, service obligations at the federal level are largely contractual in nature. *Recovery of Stranded Costs By Public Utilities and Transmitting Utilities*, 59 Fed. Reg. 35274, 35278 (July 11, 1994).

Changing jurisdiction of retail transmission from the States to FERC entails a move from the one type of regulatory framework to the other. It also shifts policy choices from state regulators to federal; and, with this shift from State Capitols to Washington D.C., invariably come changes in the kinds of policies that are favored and in the groups whose voices are most strongly heard.

A good example is close at hand. In times when transmission is short, because of equipment failure or capacity constraints, States commonly require electric utilities to protect first the retail customers to whom public utility obligations are owed (and in whose interests the utility is given its service monopoly by State law). FERC's antipathy to this policy is well known, but its attempt to override state policy by using its wholesale jurisdiction was rebuffed. *Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999), *cert. denied sub nom. Enron Power*

23. *See, e.g.*, 1935 Senate Hearings at 246 (describing Sections 202 and 204 of the bill prepared by the FPC); 1935 Senate Report at 19-20 (discussing the decision to eliminate these provisions and requirements); *Otter Tail Power Co. v. United States*, 410 U.S. 366, 383-85 (1973) (Stewart, J., concurring and dissenting) (discussing some of the Senate's changes). The authority Congress did give FERC is very circumscribed. *See* 16 U.S.C. §§ 824a(b) (FERC may not order interconnection and sale or exchange of energy that would require the electric utility to enlarge its generation facilities, or that would impair adequate service to the utility's retail customers); 824f (same limitations on FERC's authority to remedy complaint of inadequate service, and such a complaint may only be filed by a state commission).

Mktg., Inc. v. Northern States Power Co., 528 U.S. 1182 (2000). If FERC obtains jurisdiction over retail transmission facilities, however, it can implement its different policy for retail customers directly — even though it has never regulated retail service and never before claimed authority to do so.

CONCLUSION

There are policy arguments, which the Court will hear from Enron and others, that control of the electricity transmission system should be shifted to the Federal Government. The issue is not policy. It is who will decide "to displace a state regime with the federal one, since the Congress promised that as much as possible be left to the States." *Florida Power*, 404 U.S. at 476 (Douglas, J., dissenting). Congress did not confer that power on FERC, which nevertheless has claimed it. This Court should hold that only the politically responsible Branch that made the promise has authority to revoke it.

The portions of FERC's Order asserting jurisdiction over unbundled retail transmission should be vacated.

Respectfully submitted,

BILL LOCKYER
Attorney General of the State of California
PETER SIGGINS
Chief Deputy Attorney General
RICK FRANK
Chief Assistant Attorney General
MORRIS BEATUS
Senior Assistant Attorney General
1300 I Street, Suite 125
Sacramento, CA 94244-2550
(916) 445-1939

GARY M. COHEN*
General Counsel
WILLIAM JULIAN II
PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA
505 Van Ness Avenue
San Francisco, CA 94102
(415) 703-1086

* *Counsel of Record*

Attorneys for Amici Curiae the State of California and the Public Utilities Commission of the State of California

MAY 31 2001

Supreme Court, U.S.
FILED

MAY 31 2001

OFFICE OF THE CLERK

Nos. 00-568 and 00-809

In the Supreme Court of the United States

STATE OF NEW YORK, ET AL., *Petitioners*,
v.
FEDERAL ENERGY REGULATORY COMM'N, ET AL.

ENRON POWER MARKETING, INC., *Petitioner*,
v.
FEDERAL ENERGY REGULATORY COMM'N, ET AL.

On Writ of Certiorari to the United States
Court of Appeals for the District of Columbia Circuit

BRIEF *AMICUS CURIAE* OF ELECTRICAL ENGINEERS, ENERGY ECONOMISTS AND PHYSICISTS IN SUPPORT OF RESPONDENTS IN NO. 00-568

CHARLES J. COOPER
Counsel of Record
BRIAN STUART KOUKOUTCHOS
COOPER & KIRK, PLLC
Suite 200
1500 K Street, N.W.
Washington, D.C. 20005
(202) 220-9600

May 31, 2001

BEST AVAILABLE COPY

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

INTEREST OF *AMICI CURIAE* 1

SUMMARY OF ARGUMENT 1

ARGUMENT 3

I. THE PHYSICAL REALITIES OF THE TRANSMISSION OF ELECTRICITY. 5

II. THE STRUCTURE, OPERATION, AND HISTORICAL DEVELOPMENT OF THE ELECTRIC POWER SYSTEM 12

A. Structure and Operation 12

B. Development of Transmission Systems Since 1935. 17

III. THE STATE PUCS MISUNDERSTAND THE PHYSICS OF ELECTRIC ENERGY AND HOW IT IS TRANSMITTED AND THEREFORE MISAPPLY THE FPA'S "ENGINEERING AND SCIENTIFIC" TEST FOR FEDERAL JURISDICTION. 18

IV. THE STATE PUCS MISUNDERSTAND POWER SYSTEM STRUCTURE AND OPERATION AND THEREFORE MISAPPREHEND THE DIVISION OF STATE AND FEDERAL JURISDICTION UNDER THE FEDERAL POWER ACT. 26

CONCLUSION 30

TABLE OF AUTHORITIES

Cases **Page**

Berkey v. Third Ave. Ry., 224 N.Y. 84, 155 N.E. 58 (1926) 5

Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) 4, 25

FPC v. Florida Power & Light Co., 404 U.S. 453 (1972) 4, 10, 12, 22

Statutes

Federal Power Act, codified at 16 U.S.C. §§ 792 *et seq.*
§201(a) 28, 30
§ 201(b)(1) . . . . . *passim*
§ 201(c) 19, 27
§ 201(d) 27
§ 206(d) 27

Administrative Cases & Orders

Florida Power & Light Co., 37 F.P.C. 544 (1967), *aff'd, FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972) 9, 10, 12, 15, 22

Order No 888, FERC Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (May 10, 1996) 14, 18

Miscellaneous **Page**

ABB Power T&D Co., INTRODUCTION TO INTEGRATED RESOURCE T & D PLANNING (1994) . . . 13, 14

Michael Boudin, *Antitrust Doctrine and the Sway of Metaphor*, 75 GEO.L.J. 395 (1986) 5

Olle Elgerd, ELECTRIC ENERGY SYSTEMS THEORY: AN INTRODUCTION (1971) 15

Florida Reliability Coordinating Council, "2000 Regional Load and Resource Planning" (July 2000) 20

Glossary of Terms Task Force of the North American Electric Reliability Council (1996). 27

J. Duncan Glover & Mulukutla Sarma, POWER SYSTEM ANALYSIS AND DESIGN (1994) 1, 17, 18

Larry Gonick & Art Huffman, THE CARTOON GUIDE TO PHYSICS (1990) 6

P. Guedella, PALMERSTON (1927) 5

Idaho State Electricity Profile (1998), U.S. Dept. of Energy, Energy Information Admin. 20

Brian Koukoutchos, *Constitutional Kinetics: The Independent Counsel Case and the Separation of Powers*, 23 Wake Forest L.Rev. 635 (1988) 5

Bob McCaw, *The Great Blackout*, POWER ENGINEERING (Dec. 1965) 16

Syed Nasar, ELECTRIC ENERGY SYSTEMS (1996) . . 15, 17, 18

Miscellaneous **Page**

Robert Sarikas, INTRODUCTION TO ELECTRICAL THEORY AND POWER TRANSMISSION (1995) 18, 20, 25, 26

D. Sayers, THE POETRY OF SEARCH AND THE POETRY OF STATEMENT (1963) 5

William Stevenson, ELEMENTS OF POWER SYSTEM ANALYSIS (4th ed. 1982) 9, 17

B.M. Weedy & B.J. Cory, ELECTRIC POWER SYSTEMS (1998) 23

Allen Wood & Bruce Wollenberg, POWER GENERATION, OPERATION AND CONTROL (1996) 15

www.aep.com/about/territory.htm. 24

www.bpa.gov/corporate/KCC/ff/bpa_facts/page2.shtml ... 21

www.idahopower.com/company/facts.htm 21

www.pacificorp.com/paccomp/ 21

www.pjm.org 24

INTEREST OF AMICI CURIAE

Amici curiae are electrical engineers, economists, and physicists specializing in the study of electricity and the operation of electric power systems. They have an abiding professional interest in the proper regulation of the ever more important electric energy industry.[1] American dependence upon electric energy has nearly doubled in the last three decades as the nation steadily moves beyond fossil fuels. Electricity's share of U.S. primary energy use is expected to reach 46% by the year 2010. J. Duncan Glover & Mulukutla Sarma, POWER SYSTEM ANALYSIS AND DESIGN 8 (1994).

The division of state and federal regulatory jurisdiction set forth in the Federal Power Act of 1935 was deliberately drawn by Congress in accord with the scientific and engineering realities of electric power generation, transmission, and distribution. As scholars and consultants specializing in those fields, *Amici* respectfully submit this brief as an aid to this Court's understanding of those principles of physics and engineering, and their relevance to the application of the "engineering and scientific test" that Congress has prescribed for deciding questions of federal jurisdiction. Counsel of record for all parties have consented to the filing of this brief.[2]

SUMMARY OF ARGUMENT

Congress wrote the Federal Power Act ("FPA") in the language of electrical engineers and mandated that federal jurisdiction follow the flow of electric energy — an engineering

---

[1]The qualifications of and positions held by *Amici* are set forth in Appendix B, bound with this brief. *Amici* appear here in their individual capacities as scholars, scientists and engineers, rather than as representatives of the institutions with which they may be affiliated. This brief has been financed by the *Amici* with support from Dynergy, Inc., and Coral Energy. No counsel for any party authored this brief in whole or in part, nor did any party make a monetary contribution to the brief.

[2] Letters of consent have been filed with the Clerk.

and scientific, rather than a legalistic or governmental, test. Yet the state public service commissions ("PUCs") challenging FERC's jurisdiction under Order 888 misunderstand the physics of electric energy and how it is transmitted, and therefore misapply the FPA's test for federal jurisdiction.

The PUCs base their argument for restrictions on FERC jurisdiction on an inaccurate and misleading metaphor. They imagine electrons entering one end of a transmission wire at a generating plant, flowing through the wire like drops of water through a pipe, and then emerging at the other end of the wire in a lightbulb in a home. They imagine electrons as discrete items whose transmission can be controlled, directed and traced. They extend this metaphor to argue that FERC does not have jurisdiction to regulate the interstate transmission of such a stream of electrons unless it can show that every electron used by a retail customer in each state is generated in a different state.

But this is not how electricity works. *Energy* is transmitted, not electrons. Energy transmission is accomplished through the propagation of an electromagnetic wave. The electrons merely oscillate in place, but the *energy* — the *electromagnetic wave* — moves at the speed of light. The energized electrons making the lightbulb in a house glow are not the same electrons that were induced to oscillate in the generator back at the power plant.

Electric energy on an alternating current network *cannot* be addressed like a phone number or an e-mail and dispatched to a particular recipient over a prescribed and fixed pathway. Energy flowing onto a power network or grid *energizes the entire grid,* and consumers then draw undifferentiated energy from that grid. A networked electric grid flexes, and electric current flows, in conformity with physical laws, and those laws do not notice, let alone conform to, political boundaries. If the transmission lines of the system cross state boundaries, then electric currents on the system necessarily do likewise. With the exception of transmissions on the electric grids isolated in the states of Hawaii, Texas, and Alaska, *all* transmissions are interstate because *all* transmission lines are part of one of the two vast

American electric grids that span multiple state boundaries. The State PUCs' arguments to the contrary defy established principles of physics and electrical engineering.

The PUCs misunderstand power system structure and operation and therefore misapprehend the division of state and federal jurisdiction under the FPA. They try to rewrite the vocabulary for electric regulatory discourse by introducing new concepts of "retail transmission" and "wholesale transmission." These terms are fabrications that do not appear in the FPA. "Wholesale" and "retail" are transactional terms, which is why the FPA uses them only to distinguish types of *sales*. These terms have no relevance to the *transmission* of electricity.

The PUCs would like to pretend that the world has not changed since 1935. They contend that the massive increase in interstate, interconnected electric networks is not relevant to the jurisdictional issue because this change did not alter the FPA's language. The PUCs accuse FERC of trying to rewrite the FPA's jurisdictional assignments to invade the regulatory sphere reserved to the states.

There has been no change in the FPA's text or interpretation. The jurisdictional lines drawn in the FPA are still the same: the states get generation, distribution, and intrastate transmission, while FERC gets interstate transmission. What has happened is that the electrical system being regulated has changed. Interconnected networks and interstate transmissions were few and far between in 1935; today every high-voltage transmission line in the continental U.S. (outside Texas) is wired into one of the two vast interstate grids. Thus, the electrical transmission system has become inherently interstate — and has thereby grown away from the state regulatory territory defined by the FPA and grown into federal territory.

ARGUMENT

In the Federal Power Act, 16 U.S.C. § 824(b)(1), Congress allocated regulatory jurisdiction over electric energy along lines

drawn, in effect, by electrical engineers.[3] That is, the electric power industry was divided into three categories — generation, local distribution, and transmission — and the states were given jurisdiction over "facilities used for the generation of electric energy or over facilities used in local distribution," while the Federal Power Commission (now known as FERC) was given jurisdiction over "the transmission of electric energy in interstate commerce." *Id.*

Accordingly, this Court has long held that the question of federal vs. state jurisdiction under the FPA turns in large part on the physical realities of science and electrical engineering. Congress wrote the FPA "in the technical language of the electric art" and decreed that "[f]ederal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test." *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 529 (1945). Thus here, as in so many previous cases, it is an "'engineering and scientific test' that controls this case." *FPC v. Florida Power & Light Co.*, 404 U.S. 453, 467 (1972).

Amici curiae, as engineers and other experts schooled and experienced in the "electric art," submit this brief as an aid to the Court's understanding of this "engineering and scientific test." In particular, *Amici* are concerned because the parties challenging FERC's jurisdiction under Order 888 misapprehend and misrepresent the realities of the electric power system. We will first explain some of the fundamentals of physics and engineering relating to (1) the transmission of electricity and (2) the structure, operation and historical development of the electric power system. We will then apply those fundamentals to the arguments of those opposing FERC's jurisdiction.

---

[3] 18 U.S.C. § 824(a)-(e) codifies the FPA § 201(a)-(e). In conformity with the parties' practice, the FPA will usually be cited by reference to its original section numbers rather than as codified in the U.S. Code.

I. THE PHYSICAL REALITIES OF THE TRANSMISSION OF ELECTRICITY.

The State Public Service Commissions ("PUCs" or "States"), which argue for restrictions on FERC jurisdiction over the transmission of electricity, base their argument on an inaccurate and highly misleading, albeit popular, metaphor of electrons flowing down transmission wires the way water flows through a pipe or blood cells flow through a vein. Metaphors are of course familiar elements of human discourse, but care must be taken in their use. "Half the wrong conclusions at which mankind arrive," Palmerston once observed, "are reached by the abuse of metaphors, and by mistaking general resemblance or imaginary similarity for real identity." P. Guedella, PALMERSTON 226 (1927). The problem is that a metaphor can convey a multitude of properties or characteristics, and not all of them may be appropriate as resemblances to the object or concept that is being described by the metaphor.

> [I]t has to be remembered that every image is true and helpful only at its relevant point. God is, in a manner, light: but He is not a succession of wave-lengths in the prime matter . . . . [N]early all heresies arise from the pressing of a metaphor beyond the point where the image ceases to be relevant.

D. Sayers, THE POETRY OF SEARCH AND THE POETRY OF STATEMENT 284 (1963). Therefore, "[m]etaphors in law are to be narrowly watched, for starting as devices to liberate thought, they end often by enslaving it." *Berkey v. Third Ave. Ry.*, 224 N.Y. 84, 94, 155 N.E. 58, 61 (1926)(Cardozo, J.).[4]

---

[4] *See generally* Michael Boudin, *Antitrust Doctrine and the Sway of Metaphor*, 75 GEO. L.J. 395, 414-16 (1986); Brian Koukoutchos, *Constitutional Kinetics: The Independent Counsel Case and the Separation of Powers*, 23 WAKE FOREST L. REV. 635, 643-46 (1988).

The State PUCs indulge in the metaphor that electrons, like water molecules or blood cells, are discrete physical entities that flow though a transmission pipeline. Electrons are deemed to be individual products "generated" in one place by an electric dynamo, then "carried" through a transmission wire where they "mingle" with other electrons, and ultimately "consumed" by a customer to power a lightbulb or appliance. *See* State PUCs Br. in No. 00-568, at 42, 43, 43-44, 45 & nn.27-28. The States extend this metaphor to argue that FERC does not have jurisdiction to regulate the interstate transmission of such a stream of electrons unless FERC can "show that essentially every electron used by a retail customer in each state . . . is generated in a different state." *Id.* at 45 n.27. *See id.* at 43-44.

This is not how electricity works. Water pipe metaphors for the transmission of electricity are popular, *see, e.g.*, Larry Gonick & Art Huffman, THE CARTOON GUIDE TO PHYSICS 131 (1990), but misleading. The "thing" that is transmitted by the wire conduits suspended from those high-tension towers one sees is *energy*, not electrons. The State PUCs imagine electrons entering one end of a transmission wire at a hydroelectric plant, flowing through the wire like water through a pipe, and then emerging at the other end of the wire in a lightbulb in a home. But electricity is not an accumulation of electrons. It is the class of physical phenomena arising from the existence and interactions of electric charge. Electric charge is one of the fundamental properties of matter. Generators do not "generate" electrons — they do not create electrons from nothing. Nor do toasters and air conditioners "consume" electrons. Electrons are not generated or consumed — but *electric energy* is. Electrons do not "flow" — but *electric current* does.

Energy, or more precisely current, is indeed measured in terms of the net charge (that is, the electrons) flowing across an

area per unit of time.[5] However, it is not these electrons that travel at the speed of light and so transmit energy from generator to consumer. The electrons that actually move through the conducting wire, hopping from one atom to the next, pressed on by the electromotive force created at the generating plant, move much too slowly to transmit much energy. These electrons collide with atoms along the way, giving up some energy as heat (which is why an electrical appliance and the wire leading from it to the plug in the wall become warm).

This broken-field running of electrons through the conducting wire is known as drift velocity and it is quite slow — less than one inch per second, as compared to 186,282 *miles* per second, which is the speed of light and the speed at which electric *current* flows through a transmission line.[6] And in an *alternating current* ("AC") system, the dominant form of energy transmission in the United States, the flow of current reverses course sixty times a second. Therefore, the electrons *oscillate* back and forth, moving in unison one way, then back the other way, without net movement over time. Hence the movement of electrons from one atom to the next through the wire transmits little energy.

The real energy transmission is accomplished through the propagation of an electromagnetic wave. Each electron is induced, under the effect of the electromagnetic wave generated at the power plant, to repel the electron in the next atom. Assume that energy is being transmitted left to right in a wire.

---

[5] The unit of electric charge is the coulomb. The unit for electric current is the ampere, equal to one coulomb per second. The unit for all types of energy is known as the joule, and the quantity of one joule per coulomb is a volt. Finally, the unit for power, the rate of transfer of energy, is the watt, which can also be represented as the product of voltage and current.

[6] The value of 186,282 miles per second is the speed of light in a vacuum. Energy travels slightly slower in any other material such as the copper conduit of an electric transmission line.

Each electron repels its right-hand neighbor, because they are both negatively charged and similar charges repel each other.[7] This ripple effect can be envisioned as each electron elbowing its neighbor toward the next right-hand neighboring electron, which in turn elbows the next electron, and so on down the power line. The electrons move very little, merely oscillating in place, but the *energy* — the *electromagnetic wave* — moves at the speed of light. The energized electrons making the lightbulb in a house glow are not the same electrons that were induced to oscillate in the generator at the generating plant.

Consider the familiar desktop toy of five or six shiny ball bearings suspended by wires from a pair of parallel horizontal bars. You lift the ball bearing on one end and allow it to fall and strike the neighboring ball bearing, and the first bearing and all the ones in the middle remain still while the bearing at the far end of the line absorbs the energy and swings out and up. The middle ball bearings, like the electrons in a transmission wire, are instrumental in *transmitting* the energy, but they do not themselves *travel* with that energy.

The water flowing in a pipeline differs from the electric current flowing in a transmission line in other respects. Water in a pipeline flows in one direction — away from the pump station to the homes of the users. And that flow is controlled and directed by the water company's staff who open and shut valves as needed. Not so for electricity. The path taken by electric energy is the path of least resistance (as determined in accord with an equation known as Ohm's Law)[8] — or, more accurately,

---

[7] The oscillation of the electrons, initially induced by the electromagnetic wave, is also instrumental in the propagation of the wave throughout the transmission network.

[8] Ohm's Law is: I = V/R (current equals voltage divided by resistance). Thus the higher the voltage, the more current flows through a conduit of a given resistance. Strictly speaking, Ohm's Law applies to direct current (DC) systems. For AC systems such as a modern American power grid, the equation involves complex mathematics (*e.g.*, V and I are represented as

the *paths* of least resistance. When more than one path is available, the energy spreads out and flows on *each path* in inverse proportion to the electrical resistance (or impedance) of that path.

The impedance of a conducting wire varies under the influence of a number of factors, including the temperature and the diameter of the wire, but the salient point is that electrical energy on an AC network *cannot* be directed. If there is more than one path available between two points, power system operators simply do not have the ability to direct the energy from a particular generator to flow on a particular set of transmission lines to a particular user.[9] Electricity cannot be addressed like a phone number or an e-mail and dispatched to a particular recipient over a prescribed and fixed pathway. Energy flowing onto a power grid *energizes the entire grid,* and consumers then draw undifferentiated energy from that grid.

For the power system to work, all the electricity on a given network must be on the same nominal frequency (60 cycles per second in North America) and all of the power generators must be synchronized and operated in parallel while they are simultaneously energizing the common grid. William Stevenson, ELEMENTS OF POWER SYSTEM ANALYSIS 3 (4th ed. 1982). The entire system operates in "electromagnetic unity." *Florida Power & Light Co.*, 37 F.P.C. 544, 549 (1967), *aff'd FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972).

The application of the concept of electromagnetic unity to power grids is not a novel approach concocted by FERC to

---

vector values rather than scalar values and resistance is replaced by the concept of impedance). But the fundamental point remains the same.

[9] New technologies, including those known as FACTS devices, can assist operators in directing power flows to some degree, and a very small number are currently installed, for example, on the New York-New Jersey border. But their enormous cost prohibits their widespread installation for the foreseeable future.

justify the reach of Order No. 888. It is a fundamental premise of electrical engineering and it has been FERC's approach to jurisdiction over interstate transmission for at least 35 years. This Court summarized "the electromagnetic unity of response of interconnected electrical systems" in *Florida Power & Light*:

> None of the connected electric systems including that of [any particular utility] has any control over the actual transfers of power at each point of interconnection because of the free flow characteristics of electric networks . . . . An electric utility system is essentially an electro-mechanical system to which all operating generators on the interconnected network are interlocked electromagnetically. This means that electric generators, under ordinary operating conditions run either at exactly the same speed or at speeds which will result in a frequency of 60 cycles. No operating generator can change its speed by itself as long as it operates connected to the network . . . .
>
> If a housewife in Atlanta on the Georgia system turns on a light, every generator on Florida's system almost instantly is caused to produce some quantity of additional electric energy which serves to maintain the balance in the interconnected system between generation and load. If sensitive enough instruments were available and were to be placed throughout Florida's system the increase in generation by every generator . . . could be precisely measured.

404 U.S. at 460 (quoting Opinion of the Hearing Examiner, 37 F.P.C. at 567-68).

This understanding of the unity of electromagnetic response is anything but controversial. In *Florida Power & Light* itself, even the complaining utility company conceded that the approach was "technologically sound." 404 U.S. at 461-62. It

could hardly have argued otherwise, for electromagnetic unity is dictated by a set of four fundamental physical principles known as Maxwell's Equations. The import of these rules is that the sum of electrical currents flowing into any point in a circuit must equal the sum of currents flowing out, and the sum of voltages around any closed loop in a circuit must equal zero.[10]

These rules explain (1) why physical events — such as the addition of electrical energy or an increase in electrical load — cannot be isolated on an interconnected grid, and (2) why energy flowing on an interstate grid cannot be cabined within an arbitrary geographical boundary. If a generator on the grid increases its output, the current flowing from the generator on all paths on the grid increases. These increases affect the energy flowing *into* each point on the network, which in turn leads to compensating and corresponding changes in the energy flows *out* of each point. The increased generator output also affects the electromagnetic fields and the voltages on the grid, which must adjust themselves to sum to zero around all closed loops within the system. The system flexes and the current flows in conformity with physical laws, and those laws do not notice, let alone conform to, political boundaries. If the transmission lines of the system cross state boundaries, then electric currents on the system necessarily do likewise.

FERC's characterization in *Florida Power & Light* of an interconnected power grid as unified in electromagnetic response

---

[10] Maxwell's Equations explain how oscillating electric fields (fields that vary over time) induce magnetic fields, and oscillating magnetic fields induce electric fields. The role of electric generators is to create these oscillating fields. Under certain conditions two of these equations can be used to derive a more familiar pair of rules known as Kirchhoff's Laws, which are rules for analyzing electrical circuits. Kirchhoff's Current Law states that the sum of electrical currents flowing into any node (point) in a circuit must equal the sum of currents flowing out. Kirchhoff's Voltage Law, based on one of Maxwell's Equations known as Faraday's Law, provides that the sum of voltages around any closed loop in a circuit must equal zero.

was based on a large administrative record of expert testimony. 37 F.P.C. at 549-50. That was the same type of electrical expertise to which this Court deferred in accepting FERC's conclusion that electrical energy from different sources is inevitably commingled in an electrical "bus" (an interconnection between two or more facilities). *Florida Power & Light,* 404 U.S. at 463 (affirming 37 F.P.C. at 550). When resolution of a question "depends on 'engineering and scientific' considerations," this Court "recognize[s] the relevant agency's technical expertise and experience, and defer[s] to its analysis." *Id.* at 463. Indeed, the Court concluded that passing "[j]udgment upon these conflicting engineering and economic issues is precisely" why FERC was created, and therefore deference is due "'so long as it cannot be said . . . that the judgment which [FERC] exercised had no basis in evidence and so was devoid of reason.'" *Id.* at 466.

Therefore, even though this Court declined "to approve or disapprove" the unity of electromagnetic response as an alternative ground for jurisdiction in *Florida Power & Light*, *id.* at 462-63, the principles of deference relied upon by the Court to decide that case support embracing the electromagnetic response approach to jurisdiction in this case.

II. THE STRUCTURE, OPERATION, AND HISTORICAL DEVELOPMENT OF THE ELECTRIC POWER SYSTEM.

A. Structure and Operation.

An electric power system consists of three principal divisions: *generation, transmission*, and *local distribution. See* Stevenson, *supra*, at 1.

Generation takes place at a power plant where a fuel such as coal, gas, oil, uranium or hydro power is used to spin a turbine which turns a generator to generate electricity.

Transmission lines connect the generating stations to the distribution systems (and also connect the entire utility power

system to other power systems). *Id.* Transmission takes place on a network — a configuration of power lines connected so that multiple paths exist between any two points (or nodes) on the network. ABB Power T&D Co., INTRODUCTION TO INTEGRATED RESOURCE T & D PLANNING 10 (1994). This ensures reliability: if any one line fails, there is an alternate route and power is (hopefully) not interrupted. *Id.* As a result of the network arrangement, energy flows every which way on the grid, depending on where the load (demand for electricity) and generation are at any given moment, with the energy always following the path (or paths) of least resistance. Transmission is conducted at extremely high voltages — up to a million volts — because high voltage is necessary to deliver power over any significant distance. The 120 to 240 volt output of the wall sockets in an American home is insufficient to move power more than a few hundred yards. ABB Power, *supra*, at 4.

In addition to moving electricity, the transmission grid is vital to the stability of the power system. Indeed, much of the capital investment in transmission systems has traditionally been driven by the need for stability rather than the need to move power. By ensuring firm electrical ties among all generators, the grid enables even far-flung generators to stay electromagnetically synchronized with one another, which enables the system to function smoothly as the electrical load fluctuates and to pick up load smoothly if any generator fails. *Id.* at 10-11.

The *local distribution* system begins at a substation where electricity is received from the transmission lines and stepped down to a lower voltage by transformers. Simultaneously, the power flow is split to send power to a number of primary feeder lines that lead to other transformers that again step down and feed the power to secondary service lines that in turn deliver the power to the utility's customers. ABB Power, *supra*, at 6-7. Unlike the network arrangement of a transmission grid, more than 99% of all local distribution systems are designed as *radial* systems. *Id.* at 18. Radial systems are *closed* — once power is transmitted to them, it is delivered to customers. Electricity is

not stepped up in voltage and put back on the transmission grid. Because there is only a single path between each customer and the substation, the route of power flow in a local distribution system is absolutely certain. *Id.* at 19. The consequence of this simplicity in design is that a radial feeder system is not as reliable as a network; if a falling tree takes down a feeder line during a storm there is no alternate route for power delivery. On the other hand, such an outage is isolated and affects only the customers served by that particular line; neighbors on a different radial line experience no blackout. *Id.* at 19-20.[11]

The most salient feature of a contemporary power system is *interconnection* — a group of individual utility company transmission networks that are themselves networked together. Transmission networks are connected by "tie-lines" over which companies share power. Energy may be bought and sold to economize: for example, if company X's electricity is less expensive to procure at a given time than Company Y's would be to produce, Y will buy electricity from X and have it transmitted over the grid. Energy may be bought when Company A cannot meet demand by itself: for example, if A depends heavily on hydroelectric power (as many western utilities do) and the region where A is located has been experiencing a drought that lowers river levels, or if A needs to take generating equipment off-line for repair or replacement.

---

[11] Thus, transmission is distinguished from local distribution by higher voltage, network configuration, and function. ABB Power, *supra*, at 9-10. Order 888 contains a seven-factor test for distinguishing facilities used for local distribution from those used for transmission: (1) local distribution facilities are in proximity to retail customers; (2) are radial in character; (3) power flows into them but rarely, if ever, flows out; (4) power within the distribution system is not reconsigned to some other market; (5) power is consumed in a relatively confined geographic area; (6) meters are placed at the transmission/distribution interface to measure flows into the distribution system; and (7) distribution systems are of reduced voltage. Order No. 888, FERC Stats. & Regs. ¶ 31,036, 31,770, 61 Fed. Reg. 21,540 (May 10,1996).

Thus, many energy transfers on the grid are pre-arranged by agreement between the parties. But even these transfers are achieved by having the supplying utility ramp up its electrical generators and having the receiving utility either ramp its generators down or simply not interrupt the demand on the grid, with the effect that net power flow over the tie-lines is in the direction of the desired exchange. Thus, this type of exchange confirms, rather than refutes, the proposition that the grid is electrically unified.

Moreover, this describes operation of a power grid only when everything goes according to plan — which happens no more often in the electric power industry than it does in any other part of life. The utility control systems described by the PUCs "are not perfect devices, with the result that there are regularly occurring instances [of] . . . inadvertent interchange." Allen Wood & Bruce Wollenberg, POWER GENERATION, OPERATION AND CONTROL 380 (1996). When a utility gets too far out of line in consuming power beyond the power-sharing plan agreed upon with its neighbors on the grid, this is known as "leaning on the ties." *Id.* Thus, because the individual utility networks are connected by a tie-line "which permits a free flow of power and energy throughout the networks," all the contributing utilities "operate in parallel and are interlocked electromagnetically," and any given utility company on the interconnection "has no control over the actual transfers of electric power and energy with any particular electric system with which it is interconnected." *Florida Power & Light*, 37 F.P.C. at 549.

Another category of inadvertent exchange is a system disturbance — a transmission line goes down or a generator is tripped off-line suddenly and power automatically flows to the newly deficient network before intervention by a system operator is possible. Syed Nasar, ELECTRIC ENERGY SYSTEMS 319 (1996). In such emergencies, the rotor dynamics of the various electrical generators linked on the interconnection are uncontrolled. Olle Elgerd, ELECTRIC ENERGY SYSTEMS THEORY: AN INTRODUCTION 478-79 (1971).

Finally, energy flows across the tie-lines that interconnect separate utility networks in uncontrollable ways due to parallel or loop flows. The problem is that the "contract path" for the electrical transmission agreed upon by the buyer and seller in negotiating the transaction has nothing to do with the route by which the power actually flows. Electrical energy follows the path of least resistance on the grid. The flow of energy is therefore said to be on a different "loop" of transmission lines, which are parallel (electrically speaking, *not* geographically) to the nominal "intended" path. Thus, the exchange of power may have been planned, but the route (or routes) that the energy took across the tie-lines of the grid was not planned — nor could it have been. This form of electrical interchange is up dramatically in recent years due to the growth in energy market transactions spurred by the advent of deregulation.

The structural, engineering differences between network-configured transmission systems and radially configured local distribution systems have important implications. On a network, events cannot be isolated. A physical event anywhere on a grid — a downed transmission line, a failed relay switch, a large generator coming on line — affects every other point on the network.

Perhaps the most dramatic illustration of this was the Great Northeast Blackout of 1965. *See* Bob McCaw, *The Great Blackout*, POWER ENGINEERING 36A-36C (Dec. 1965). When a single relay at a power plant in Ontario, Canada was set incorrectly on November 9, 1965, the 300 megawatt load being carried on the line controlled by that relay was immediately dumped onto the other lines emanating from that plant and they all tripped out, even though they were not overloaded. The 1600 megawatts being carried by those lines into Ontario were suddenly dumped on the New York system, and the resulting power surge knocked out the main east-west transmission line and a series of cascading tripouts shut down seven units that had been feeding the Northeast grid. The consequent drain on systems to the south (New York City) and the east (New

England) caused the whole system to collapse. The remaining plants could not handle the demand and as their generators struggled to make up the lost supply of electricity, automatic safeties shut down those plants to save them from damage. Loss of the upstate power plants caused an immediate, convulsive reversal of energy flow: for example, New York City, which had been drawing 300 megawatts from the network, now was trying to power not only the City but much of the rest of the state. At the height of the evening rush hour, darkness descended as thirty million people in eight states plus eastern Canada were blacked out.

It is therefore undeniable that the entire transmission network of a given interconnection must be operated cooperatively as one big, synchronized system. The North American Electric Reliability Council (NERC) was created as a voluntary industry organization in response to the 1965 blackout, with the goals of preventing such events through improved communication and coordinating the industry response when such events occur. NERC exists precisely because of the inescapable interdependence of the electricity network.

B. Development of Transmission Systems Since 1935.

Both Enron and the State PUCs agree that when the FPA was enacted in 1935, electricity was essentially a local business. State PUCs Br. in No. 00-568, at 27; Enron Br. at 6. *See* J. Duncan Glover & Mulukutla Sarma, POWER SYSTEM ANALYSIS AND DESIGN 7 (1994) (utilities were isolated systems); Nasar, *supra*, at 319 (originally limited to radial feeder systems for single towns); Stevenson, *supra*, at 2-3 (individual, isolated systems). The parties also agree that in 1935 only a fraction of America's electric systems were interconnected across state lines and consequently the vast majority of electrical transmissions were entirely intrastate. Enron Br. at 7; State PUCs Br. as Resp. in No. 00-809, at 26 (over 80% of transmissions were intrastate). Indeed, the first instance of two large power systems actually

operating with an interconnection for a meaningful period of time did not occur until 1926, and even that operation was entirely intrastate. Nasar, *supra*, at 319. It is therefore unsurprising that interstate transmission was still in its infancy when Congress enacted the FPA in 1935.

As interconnection among neighboring utilities grew, *see* Glover & Sarma, *supra*, at 7-8, largely due to the pursuit of greater reliability and to technology that made transmission possible over longer distances with higher voltage, power companies isolated within a single state became virtually extinct. With the exception of some companies in Texas, *every* utility in the continental United States, coast-to-coast, is grouped into one of nine regions called Electric Reliability Councils that in turn constitute two huge interconnected networks: (1) Midwest and Eastern U.S. and (2) Rocky Mountains and Western. *See* Robert Sarikas, INTRODUCTION TO ELECTRICAL THEORY AND POWER TRANSMISSION 79-80 (1995). *All* transmission lines (outside the three states listed above) are connected to one of these two interstate grids. Order No. 888, at 31,781.

A map of the North American high voltage transmission system is included in Appendix A at A-1. If the transmission grid conformed to political borders, one could easily discern the boundaries of the 48 states. But as the second map at App. A-2 shows, without an overlay of the borders, a map of transmission lines is useless for defining even the American-Canadian frontier, much less the state borders. The transmission grid is interstate — indeed, inter*national* — and so is the electricity on that grid.

III. THE STATE PUCS MISUNDERSTAND THE PHYSICS OF ELECTRIC ENERGY AND HOW IT IS TRANSMITTED AND THEREFORE MISAPPLY THE FPA'S "ENGINEERING AND SCIENTIFIC" TEST FOR FEDERAL JURISDICTION.

Section 201(b)(1) of the FPA grants FERC jurisdiction over "the transmission of electric energy in interstate commerce," and

section 201(c) provides that "electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof." 16 U.S.C. §§ 824(b)(1) & 824(c). Accordingly, the issue of federal jurisdiction becomes primarily a question of physics and electrical engineering: is energy transmitted on an interconnected grid that spans state borders transmitted from one state and consumed outside it?

With the exception of transmissions on the electric grids isolated in the states of Hawaii, Texas, and Alaska, *all* transmissions are interstate because *all* transmission lines are part of either the "Midwest and Eastern" or "Rocky Mountains and Western" interconnections. *See* App. A-2. Those interconnections span multiple state boundaries, and every watt of power generated in their territory is fed onto a network where it becomes part of a single, synchronized, inherently multi-state, electromagnetic waveform, from which undifferentiated electric energy is drawn and consumed by customers in every state on that interconnection. The State PUCs' arguments to the contrary defy established principles of physics and electrical engineering.

1. The State PUCs insist that "[m]ost electricity used in the U.S. is generated in the state where it is used." State PUCs Br. in No. 00-568, at 5. The only support proffered for this assertion is several statistical reports describing energy use in New York, Florida, and Idaho. Those reports do not even purport to confirm the State PUCs' assertion, nor could they, since all three states are on multi-state interconnections and there is simply no telling where the energy generated in those states goes once it is on the grid. Those reports establish, at most, only that these states each generate as much power every year as they consume. That may make these states annually self-sufficient in some bookkeeping sense. But that does not change the fact that, in the day-to-day operations of the utilities in these states, they are continuously interconnected with a unified interstate network energized by a single electromagnetic waveform. From a financial or

transactional perspective, records are kept as to whether each utility is carrying its own weight and meeting its obligations under the complex power-sharing contracts that are a requirement for connection to the network. But from the perspective of physics and electrical engineering, once a company's generators are wired into the grid the energy on that interstate network cannot be differentiated in ownership or origin. Thus, simply to be a member of a multi-state power network is to participate in interstate commerce in electricity.

Indeed, both the Florida and Idaho reports cited by the PUCs reveal that those states are in fact "Net Importers" of electricity. Idaho State Electricity Profile (1998), U.S. Dep't of Energy, Table 1; Florida Reliability Coordinating Council, "2000 Regional Load and Resource Planning" 33 (July 2000). The very fact that these statistical tables record "net" figures for electrical exchange with sources in other states confirms that Florida and Idaho — like 45 other states — routinely transmit power to, and consume power from, other states.

Actually, Idaho is an egregiously poor example for the "self-contained states" point the PUCs are trying to make, because that state might well qualify as the poster child for interstate interconnections. Idaho is part of not one, but *four* different interstate electrical control areas. The function of a control area is moment-to-moment regulation of the energy on the control area's network through "instantaneous matching of generation and load so as to maintain constant frequency and synchronous time." Sarikas, *supra*, at 69. Control areas also maintain energy accounts for financially settling the energy exchanges that flow back and forth among the utilities that are members of the control area. From an engineering perspective, control areas are the electric power system's jurisdictional entities.

The problem for the State PUCs is that the political borders of the State of Idaho do not constitute such a control area. Instead, Idaho's power system is balkanized into four different control areas, each of which covers part of Idaho and parts of other states as well. The PacifiCorp West control area includes

one part of the western border of Idaho — along with parts of California, Oregon, Washington, and Nevada. *See* www.pacificorp.com/paccomp/. PacifiCorp East includes southeastern Idaho — and most of Utah and parts of Wyoming. *Id.* The Idaho Power control area includes most of the central parts of the state — as well as parts of Oregon and Nevada. *See* www.idahopower.com/company/facts.htm. Finally, the Bonneville Power Authority control area includes much of northern Idaho — as well as portions of Oregon, Washington, Wyoming, Nevada, Utah, California, western Montana, and eastern Montana (but not central Montana). *See* www.bpa.gov/corporate/KCC/ff/bpa_facts/page2.shtml.

Thus the moment-to-moment operations and energy transfers of any given electric company in Idaho are controlled in parallel *not* with the other utilities throughout Idaho, but with utility companies in that electric company's *control area*, which may encompass as many as *seven other states*.

2. The States assert (without citation to any authority) that "most energy passes from power plants to the retail customers who are first in line on transmission lines with suitable capacity." State PUCs Br. in No. 00-568, at 45 n.28. *See also id.* at 37 (same). Once again, the States rely on their erroneous model of "electrons" being "carried" here and there in discrete, traceable units, like drops of water in a pipeline. *Id.* at 45. The resulting fallacy is the assumption that, because electric energy is generated and electric energy is consumed within a state, this energy can be treated as though it were somehow identifiable as the *same* energy — as if it were somehow distinguishable from the rest of the undifferentiated electromagnetic wave that was electrifying the interstate grid at the moment the user flipped on his television set. Again, that is not how electricity works.

Unsurprisingly, the State PUCs' argument has already been rejected by this Court. In *Florida Power & Light*, the FP&L utility claimed that, even though it was on a grid that crossed into Georgia, it somehow knew that all of its wattage was exhausted

by its own nearby users (or those of a neighboring Florida utility) "before the point, further down the line, where Georgia's load intervenes." 404 U.S. at 462. The dissent accepted the utility's argument, 404 U.S. at 471-72 (Douglas, J., dissenting), but the majority did not. FERC's expert conclusion that energy from multiple, multi-state sources "commingles in a bus" at the interconnection and is then "transmitted in commerce" was sufficient to confer federal jurisdiction under the FPA. 404 U.S. at 463.

3. The PUCs offer no proof that the power they generate and transmit on an interstate network nevertheless is consumed solely by in-state customers. But nothing would change if they made such a proffer because this Court has already rejected such tracing efforts as misguided. In *Florida Power & Light,* FERC rebutted the theory of "point-to-point tracing" of alternating current electric power, noting that it was inappropriately based on "principles of direct current [DC] circuits with static power sources and with steady state power flows," and erroneously assumed power flow through an interconnection was "constant in value and direction." *Florida Power & Light Co.*, 37 F.P.C. at 551. Therefore, the theory did "not fully or accurately reflect . . . the physical reality" of an AC electric power system. *Id.* On appeal, this Court confirmed that, "'where the utility is a member of a combination of utilities and has continuous access to an integrated pool of interstate energy, the tracing of out-of-state energy is indeed difficult, burdensome, and perhaps impossible.'" 404 U.S. at 468 n.18.

4. The PUCs contend that to establish federal jurisdiction over interstate transmissions, "FERC would have to show that essentially every electron used by a retail customer in each state (other than Hawaii, Texas, and Alaska) is generated in a different state." State PUCs Br. in No. 00-568 at 45 n.27. But as explained above, electricity is not a stream of discrete electrons that travel to consumers to be individually consumed; it is not

electrons that flow through transmission wires, but electric *current*. And the current generated by all the power plants hooked up to a given multi-state interconnection energizes the entire transmission grid with one single, continuous electromagnetic waveform that by its very nature moves in interstate commerce.

5. The States argue that "all generation on the interconnected grid does not serve all customers on the grid," citing B.M. Weedy & B.J. Cory, ELECTRIC POWER SYSTEMS 175 (1998). State PUCs Br. as Resp. in No. 00-809, at 26. Professors Cory and Weedy were discussing control area operations and the management of power and frequency. But the very existence of control areas negates the States' argument. If energy flows on the grid were as discrete and containable as the States contend, then there would not be a need for control area operators to balance supply and demand for their region or to monitor both planned and inadvertent energy flows on the interfaces between control areas.

Indeed, the cited section from Weedy and Cory stresses the fluid interdependence of networked systems, by pointing out that if the electrical load (demand) changes in one company's system, the frequency of the electromagnetic wave on that system and on every other interconnected control area changes. Thus, as the authors demonstrate, if the power system in New York City were isolated from external supplies of electricity, the frequency of the electricity on the system would rapidly decline from the required 60 cycles per second and the City would be blacked out within minutes. Weedy & Cory, *supra*, at 174.

The State PUCs' premise that state power systems are self-contained explodes upon examination of the geographic outline of almost any control area in the nation, because *electric power system control areas do not respect state borders*. As explained above, Idaho is carved up among four control areas, each of which spreads into two or more other states. The PJM Interconnection spans Pennsylvania, New Jersey, and Maryland,

yet excludes a large area in central Pennsylvania. *See* www.pjm.org. The American Electric Power control area snakes like a gerrymandered congressional district through the States of Michigan, Indiana, Ohio, Kentucky, Tennessee, Virginia, and West Virginia. *See* www.aep.com/about/territory.htm. Thus, it is simply impossible to contain electricity on the grid within state borders because that electricity is generated, transmitted, and managed within control areas that are not drawn in accord with state boundaries.

6. The PUCs ultimately retreat and admit that the proposition that all transmissions "affect the entire grid" is "arguably accurate, from a theoretical standpoint" and is "technically correct." State PUCs Br. as Resp. in No. 00-809, at 25. The PUCs then fall back on the contention that any such effect is "inconsequential" because the "reaction of distant electrons in the grid is immeasurable." *Id.* The PUCs offer this example: "When a customer in New York City turns on a 60 watt lightbulb, the energy required to light the bulb is supplied by increases in output of nearby New York City generators." *Id.*

It is true that a lightbulb turned on in New York City will not have an appreciable effect on a generator very far away. It is also true that it will have almost no effect on even the closest generator. Indeed, a lightbulb or any other small device will have no effect on anyone except for the people in the room. But any event of note, such as a large industrial plant coming on line, or a large building such as the World Trade Center turning on all of its equipment, will ripple across transmission lines to affect generators both near and far, within New York and without.

7. The PUCs' concession that the premise of unity of electromagnetic response on a grid is "technically correct" is fatal to their cause, and the impact of their concession is not diminished by their qualifier that the ripple effect on a network is supposedly "inconsequential." For it is well established that there is no de minimis exception to federal jurisdiction over

interstate transmissions, no minimum threshold of megawatts. "We do not find that Congress has conditioned the jurisdiction of the Commission upon any particular volume or proportion of interstate energy involved, and we do not . . . supply such a jurisdictional limitation by construction." Connecticut Light & Power Co., 324 U.S. at 536 (jurisdiction based on "one-fifth of one per cent of all the energy received and generated" by the company throughout entire state was transmitted interstate). "If [Congress] thinks the Commission is over-extending its attention to trivial situations it has ready means of control in its hands." *Id.* at 536.

8. The States retreat even further, falling back on the contention that, even if a transmission anywhere on a network affects the unified, interstate electromagnetic wave, "these indirect reactions do not occur in radial (direct line) delivery systems designed to serve retail load." State PUCs Br. in No. 00-568, at 45 n.28. But this proves *our* point: the PUCs have confused transmission on an interconnected, *interstate network*, where events cannot be isolated (and where FERC has jurisdiction), with *local distribution* on a *radial delivery system*, where events are isolated by the system's design (and where the states have jurisdiction). *See Connecticut Light & Power Co.*, 324 U.S. at 518, 530 (federal jurisdiction follows interstate electric flow, and therefore reaches "interstate power pool" existing on network among states, but does not reach systems of "local distribution").[12]

---

[12] The PUCs' twice cite Sarikas, *supra*, at 70, 82, for the proposition that locally generated electricity is consumed locally even when transmitted on a network with interstate connections and that local events have no impact elsewhere on a network. *See* State PUCs Br. in No. 00-568, at 45-46 n.28; State PUCs Br. as Resp. in No. 00-809, at 25. But the quoted passage states only that a utility "that is generating only to meet its own requirements will have zero net interchange and will not be a net seller or buyer." True enough, but so what? The very fact that the passage refers to *net* interchanges indicates that *the utility is engaged in interchange*

IV. THE STATE PUCs MISUNDERSTAND POWER SYSTEM STRUCTURE AND OPERATION AND THEREFORE MISAPPREHEND THE DIVISION OF STATE AND FEDERAL JURISDICTION UNDER THE FEDERAL POWER ACT.

1. The PUCs confuse transmission with local distribution. For example, they purport to refute the proposition that *transmission* falls within federal jurisdiction by emphasizing that, on the contrary, "'electric current *distributed* is subject exclusively to the jurisdiction of the State.'" State PUCs Br. as Resp. in No. 00-809, at 11 (emphasis added). They answer the statement that events on an interconnected *transmission network* cannot be isolated with the pointed rejoinder that such "indirect reactions do not occur in *radial* (direct line) *delivery systems*." State PUCs Br. in No. 00-568, at 45 n.28 (emphasis added). But as explained on page 25 above, network transmission and radial distribution are fundamentally different systems, and FERC is asserting jurisdiction only over interstate transmission, in accord with § 201(b)(1) of the FPA, and not over local distribution.

2. The State PUCs try to rewrite the vocabulary for electric regulatory discourse by introducing new concepts of "retail transmission" and "wholesale transmission." *See*, *e.g.*, New York PUC Cert. Pet. at 2; State PUCs Br. as Resp. in No. 00-809, at 4, 5, 10, 17, 24, 25, 26, 27; State PUCs Br. in No. 00-568, at i, 26, 28. The States apparently believe that smuggling the term "retail" into the case in association with "transmission"

---

transmissions on the network, but that at the end of the relevant accounting period the *net* exchange is zero. The fact that the utility may thus be "self-sufficient" in some accounting sense and in some time frame, does not negate the fact that, by virtue of being interconnected, it constantly exchanges power on an interstate network, one moment taking power from the grid, the next moment adding power to the grid. Dr. Sarikas points out in the same section that every utility in America, outside Texas, Hawaii, and Alaska, is part of an interstate transmission network. *See id.* at 79-80.

will aid them in their effort to persuade this Court that Congress ousted FERC from the jurisdiction over interstate transmission explicitly conferred by FPA § 201(b)(1) by, supposedly, "implicitly recogniz[ing] the states' jurisdiction over retail transmission" in § 206(d). State PUCs Br. as Resp. in No. 00-809 at 6. *See also id.* at 7, 26. Perhaps the PUCs' hope is that "retail transmission" will sound inherently local and therefore appropriate for state rather than federal regulation.

Of course, the term "retail transmission" does not appear in the FPA, which is why the PUCs refer to the statute's supposed preservation of this power as "implicit," and why the PUCs repeat their newly coined term frequently in an effort to make it sound familiar. But the only distinction the FPA makes with respect to transmission is between in*ter*state and in*tra*state, with federal jurisdiction over the former and state jurisdiction over the latter. *Compare* § 201(c) *with* §201(b)(1). "Wholesale" and "retail" are transactional terms, which is why the FPA uses them only to distinguish types of *sales*. *See* §§ 201(b)(1), 201(d). These terms have no relevance to the transmission of electricity.[13]

Unable to locate their new vocabulary in the statute, the State PUCs attempt to give it respectability by purporting to derive the terms "retail transmission" and "wholesale transmission" from the Glossary of Terms Task Force of the North American Electric Reliability Council (1996). *See* Cert. App. Q to the NY Pet. at Q-3, Q-4. Appendix Q states (at Q-1 n.1) that the terms it sets forth have been "selected and adapted" from the official NERC Glossary of Terms, but neither of the terms in Appendix Q ("retail transmission service" and "wholesale transmission service") appears anywhere in the actual

---

[13] Perhaps the wholesale/retail distinction for sales had some utility as shorthand in 1935 for discussing transmission and distribution, because at that time wholesale sales corresponded to transmission and retail sales to local distribution. *See* NY Cert. App. C-27 (opinion below). But that neat correspondence no longer applies in the 21st century. *See* C-28.

NERC Glossary. Indeed, there is no term even referring to "retail" or "wholesale" in any way. The PUCs' portrayal of the structure of the electric power system and its implications for federal jurisdiction is therefore not only unpersuasive, it is utterly baseless.

3. The PUCs argue that, because the states regulated "retail transmission" in 1935, and because Congress intended the FPA to preserve pre-existing state regulation, the states continue to have jurisdiction over "retail transmission." In the first place, as explained above, what the FPA reserved to states was regulatory power over "the transmission of electric energy in *intrastate* commerce." FPA § 201(b)(1) (emphasis added). The category of "retail transmission," which the PUCs describe as far broader than "intrastate" transmission, is the PUCs' own invention.

The existence of section 201(b)(1) of the FPA is awkward for the PUCs' argument, so they instead invoke section 201(a), which states that "Federal regulation [shall] extend only to those matters which are not subject to regulation by the States." State PUCs Br. as Resp. in No. 00-809, at 6. *See also id.* at 5, 12; State PUCs Br. in No. 00-568, at 27-28. But that section likewise does not mention "retail transmission." The PUCs therefore devote most of their energy to arguing that the legislative history of the FPA is replete with congressional reassurances that state jurisdiction would be preserved whenever possible and that the new federal jurisdiction would be limited to those matters which cannot effectively be regulated by the states themselves. State PUCs Br. in No. 00-568, at 17-26; State PUCs Br. as Resp. in No. 00-809, at 7-12. Therefore, we are told, reading the FPA to give control over "retail transmission" to FERC would be inconsistent with the FPA's legislative purpose.

But there is no inconsistency at all. Section 201(a) formally "declare[s]" that "Federal regulation of matters relating to . . . the transmission of electric energy in interstate commerce . . . is necessary in the public interest." The next section then unambiguously grants FERC jurisdiction over "interstate"

transmission while reserving to the states most jurisdiction over "generation," "local distribution," and "intrastate" transmission. FPA § 201(b)(1). Thus those local matters subject to effective regulation by the states are still within the state bailiwick, whereas *interstate* transmission, plainly beyond *any single state's* control, is to be regulated by FERC.

When enacting the FPA in 1935, Congress could give FERC jurisdiction over all interstate transmission and simultaneously proclaim that the new statute would not, in fact, erode state regulatory power, *because in 1935 there was hardly any interstate transmission.* The federal government received jurisdiction only over what the states could not regulate effectively — *which in 1935 was not much*, given that the nation's electric power industry was almost entirely local and isolated, and electric transmission was overwhelmingly *intra*state. *See supra* pages 17-18. Thus, in 1935 the regulatory jurisdiction that the FPA conferred upon FERC constituted a relatively small portion of the total regulatory power exercised over the electric power industry.

4. The State PUCs would like to pretend that the world has not changed since 1935. They contend that increased "interconnections since 1935 are not relevant to the states' jurisdiction over retail transmissions." State PUCs Br. as Resp. in No. 00-809, at 26. Such changes, they argue, "do not alter the FPA's language." *Id.* The PUCs accuse FERC of trying to rewrite the FPA's jurisdictional assignments to invade the regulatory sphere reserved to the states.

There has been no change in the FPA's text or interpretation. The jurisdictional lines drawn in the FPA are still the same: the states get generation, distribution, and intrastate transmission, while FERC gets interstate transmission. What has happened is that the electrical system being regulated has changed. It has shifted underneath the FPA's jurisdictional lines as high-voltage interstate transmission wires have grown like new nerve fibers across the American landscape. Interconnected networks and

interstate transmissions were few and far between in 1935; today every high-voltage transmission line in the continental U.S. (outside Texas) is wired into one of the two vast interstate grids. Thus the electrical transmission system has grown away from the state regulatory territory defined by the FPA and has grown into federal territory.

As the States point out, Congress foresaw this trend to increased interstate interconnections when it drafted the FPA in 1935. State PUCs Br. as Resp. in No. 00-809, at 26. Congress accordingly defined FERC's jurisdiction in terms that would allow it to match the need for effective regulation even as the industry changed. By unambiguously providing for federal jurisdiction over "the transmission of electric energy in interstate commerce," FPA § 201(b)(1) — rather than retail transmission, wholesale transmission or some other subset of interstate transmission — Congress ensured that no gaps would develop in federal jurisdiction as the transmission system evolved. In 2001, even more than in 1935, federal regulation of this interstate commerce "is necessary in the public interest." FPA § 201(a).

CONCLUSION

For the reasons given above, *Amici curiae* urge this Court to uphold federal regulatory jurisdiction over transmissions on the nation's interconnected, multi-state electricity networks.

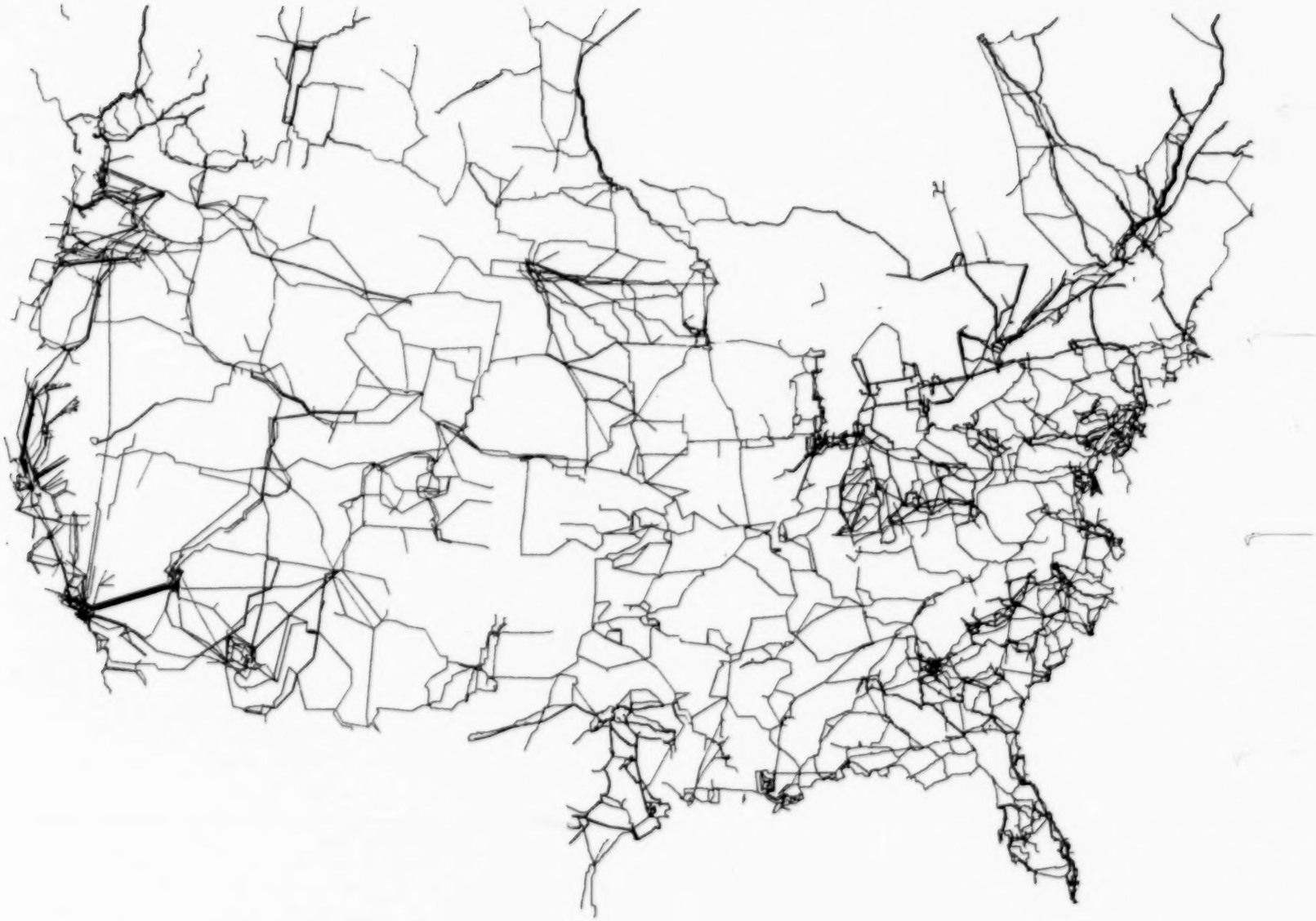
Respectfully submitted,

CHARLES J. COOPER
Counsel of Record
BRIAN STUART KOUKOUTCHOS
COOPER & KIRK, PLLC
Suite 200
1500 K Street, N.W.
Washington, D.C. 20005
(202) 220-9600

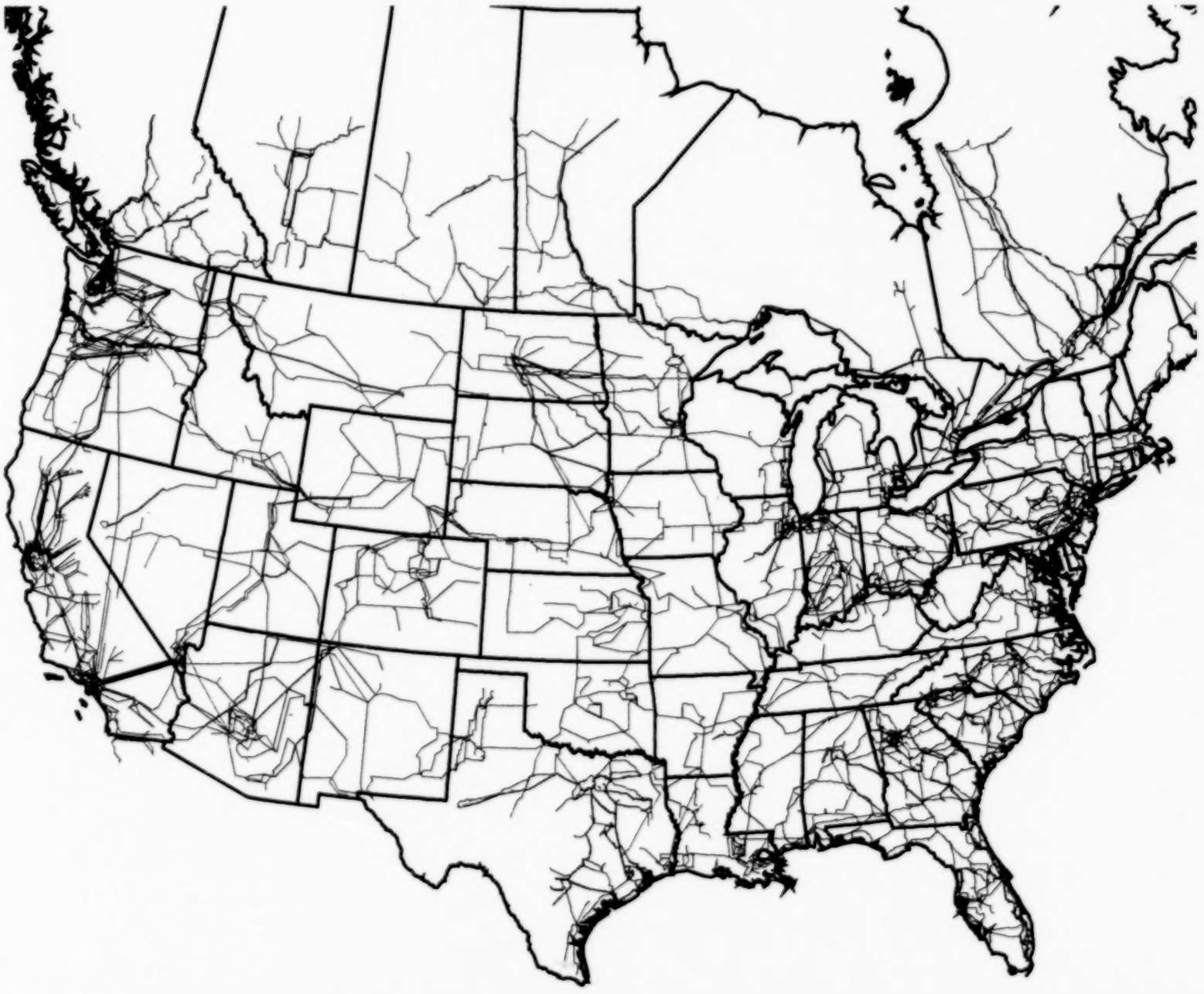
May 31, 2001

APPENDIX A

High Voltage Transmission System: USA and Canada



High Voltage Transmission System: USA and Canada with State and Provincial Boundaries



APPENDIX B

AMICI CURIAE

FERNANDO L. ALVARADO is professor of Electrical and Computer Engineering at the University of Wisconsin at Madison. A professional engineer and computer scientist, Professor Alvarado is an established leader in technical policy elements of the electric power industry. His areas of expertise include policies for market design and power system operation and power system security and stability issues in interactions between power systems. He is the author or coauthor of more than 80 technical journal publications, books and book chapters, and almost 200 conference presentations and reports. Professor Alvarado is a member of the IEEE, the Society for Computer Simulation (SCS) and the Society for Industrial and Applied Mathematics (SIAM), as well as vice chairman of the IEEE Energy Policy Committee. He earned his Bachelor of Science in Electrical Engineering at the National University of Engineering in Lima, Peru, his Master of Science in Electrical Engineering from Clarkson College of Technology, and his Ph.D in Computer, Information and Control at the University of Michigan at Ann Arbor.

CLINT ANDREWS, P.E., Ph.D., is an assistant professor in the Bloustein School of Planning and Public Policy at Rutgers University. He was educated at Brown and MIT as an engineer and planner. Previous experience includes working in the private sector on energy issues, helping to launch an energy policy project at MIT, and helping to found a science policy program at Princeton. He is Vice President of the Society on Social Implications of Technology of the Institute for Electrical and Electronics Engineers (IEEE); he is a member of the IEEE-USA Energy Policy Committee and the IEEE Power Engineering Society System Economics Committee, a past consultant to numerous electric utilities and their regulators, and an active energy policy researcher. He has authored three books. In 2000, he received a *3rd Millenium Medal* from the IEEE for contributions at the interface of technology and society.

SHIMON AWERBUCH has 30 years of experience in finance, regulatory economics, energy economics and economic development, involving the private sector and all levels of government. Dr. Awerbach has served as Chief of Economic and Policy Studies for the Utility Intervention Office of the NY State Executive Department. He has also served with the Management Consulting Service of Ernst & Young and held policy positions with the NY State Governor's Economic Development Board and the NY State Legislature. He has contributed over 50 articles to such journals as the *American Economic Review*, *Journal of Regulatory Economics* and is a member of the Editorial Board of *Energy Policy*. He is the co-author of *Independent Transmission Companies: Unlocking the Benefits of Electricity Restructuring* (PUR, November 1999) and the co-editor of *The Virtual Utility: Accounting, Technology and Competitive Aspects of the Emerging Industry* (Kluwer, 1997). He has also presented his research findings to delegates of the *United Nations Commission on Sustainable Development* in New York and has testified extensively in regulatory proceedings. Dr. Awerbach received his Ph.D. in Urban-Environmental Studies from Rensselaer Polytechnic Institute.

JUDITH B. CARDELL is an electrical engineer and policy analyst with 10 years of experience in modeling and analyzing electric power systems and electricity markets. Currently a Senior Associate with Tabors Caramanis & Associates, Dr. Cardell also spent several years as an economist and engineer for FERC. Dr. Cardell previously worked at the MIT Laboratory for Electromagnetic and Electronic Systems, and was a graduate instructor at MIT for power systems and energy policy courses. A member of the IEEE's Energy Policy Committee, Dr. Cardell has published articles on energy policy and electric market modeling. Dr. Cardell earned her Ph.D. in Technology Management and Policy from MIT's Department of Electrical Engineering and Computer Science.

BRIAN CORY is Professor Emeritus in Electrical and Electronic Engineering at Britain's Imperial College in London, where he taught for almost 40 years until 1993. Dr. Cory's research interests have been focused on virtually all aspects of electrical energy supply, including both operating systems issues as well as policy issues in the deregulation and privatization of Britain's electricity industry. In the last five years alone, he has published close to a dozen professional journal articles on topics ranging from the pricing of electricity transmission and distribution to optimizing pumped storage generation, as well as a critical review of Great Britain's reorganized electricity supply industry and a proposal for neural-network based methods for evaluating power system voltage stability.

PETER CRAMTON is Professor of Economics at the University of Maryland and President of Market Design Inc. For several electric utilities, Professor Cramton has led the auction designs for generation asset divestiture, standard offer service, and NUG entitlements under power purchase agreements. He has advised ISO New England on the design of New England's wholesale electricity market. He has also advised numerous e-commerce market makers on market design for business-to-business trading. He has served as an auction advisor in spectrum auctions for many companies worldwide, as well as the FCC, the U.S. Department of Justice, and several foreign governments. Before joining the University of Maryland faculty in 1993, he was an Associate Professor at Yale University and a National Fellow at the Hoover Institution at Stanford University. He has published numerous articles on auction theory and auction practice in major journals. Professor Cramton received his B.S. in Engineering from Cornell University and his doctorate in Business from Stanford University.

DAVID HAYWARD is an electrical engineer with a long career in the electric utility industry, specializing in power systems operation. Mr. Hayward worked at New England Electric System for close to 40 years, where he held a number of key positions in bulk power system operations. He worked as a Power System Dispatcher, then spent several years doing long range system planning and performing transmission network analysis studies. He served on the committees that analyzed the 1965 Northeast Blackout. Mr. Hayward is a Senior Member of IEEE and has served on a number of regional and national IEEE committees. He is a former Chairman of the Current Operating Problems Subcommittee (COPS) and a former member of CIGRE. Mr. Hayward has a BS in Electrical Engineering from Tufts University and is a graduate of the Greater Boston Executive Program at the MIT Sloan School.

ERIC HIRST is an independent consultant focusing on issues related to restructuring the U.S. electricity industry. He holds a doctorate in Mechanical Engineering from Stanford University. For 30 years (1970 through 2000) he worked at Oak Ridge National Laboratory, rising to the position of Corporate Fellow, a distinction shared by only 1% of the lab's technical staff. He has published almost 500 articles in the technical and semi-technical literature related to energy efficiency, utility resource planning, transmission adequacy and planning, generation adequacy, system operations, wholesale markets, and other issues related to the changes underway in the U.S. electricity industry.

JOHN B. HOWE is Vice President of Electric Industry Affairs for American Superconductor Corporation, a leading developer and manufacturer of superconductor technology for the electric power industry. Previously, he served as Chairman of the Massachusetts Department of Public Utilities (now the Department of Telecommunications and Energy), where he

spearheaded early stages of the effort to restructure and introduce retail competition to the state's regulated energy industries. Mr. Howe was also formerly a Vice President with U.S. Generating Company (now PG&E Generating Company). He has held leadership positions in the National Association of Regulatory Utility Commissioners, the New England Conference of Public Utility Commissioners, and several national and regional independent power industry organizations. He holds a B.A., Magna Cum Laude in Political Science from Amherst College and a Master of Arts in Law and Diplomacy, with a concentration in Energy and Resource Economics, from Tufts University's Fletcher School of Law and Diplomacy.

JAMES L. KIRTLEY is Professor of Electrical Engineering at MIT, where he has specialized in the development and analysis of electric machinery for 30 years. He is also Vice President and Chief Scientist at SatCon Technology Corporation, and has held positions with the Swiss Federal Institute of Technology, General Electric and Raytheon. A Fellow of the Institute for Electrical and Electronic Engineers, Dr. Kirtley is Editor in Chief of IEEE's Transactions on Energy Conversion and was the recipient of IEEE's Third Millennium Medal in 2000. He has published 45 professional journal articles, numerous conference papers, and been awarded 17 U.S. patents. Dr. Kirtley received his undergraduate, masters, and doctoral degrees in Electrical Engineering from MIT.

RALPH D. MASIELLO holds a doctorate in Electrical Engineering from the Massachusetts Institute of Technology where he worked on some of the first applications of modern control and estimation theory to electric power systems, as well as state estimators for Transmission Operations. Since then, Dr. Masiello has acquired over 20 years of experience in Transmission and Distribution Operations, having been involved in the implementation of control systems at many of North

America's largest utilities. In addition he has assisted in the design and set up of deregulated energy markets across the United States and around the world. He is currently Senior Vice President of Caminus Corporation, a leading provider of software solutions and strategic consulting to entities participating in competitive energy markets. He was formerly the global Business Unit manager for Energy Information Systems for ABB, as well as marketing manager for ABB Information Systems Division, and General Manager of ABB's Systems Control Division in Santa Clara. Dr. Masiello has been an adjunct professor at the University of Minnesota and lectured at University of California at Berkeley, the University of Arizona, and the University of Wisconsin. He is a Fellow of the IEEE and has held several committee, advisory and editorial positions within IEEE and authored numerous technical papers.

HYDE M. MERRILL is the founder of Merrill Energy LLC, which provides advanced risk, engineering, and economic analyses for participants in modern energy markets. He is currently leading a major study of power plant reliability and market behavior for a US ISO. He has advised the Peruvian Tariff Commission on transmission planning, standards, economic and institutional issues associated with competitive power markets, as well as being a member of an international consortium guiding the creation of a power pool in Southern China. Dr. Merrill organized a team that assessed market risks in four US regions, as well as advising on a Quebec commission charged with investigating the massive power losses in the Province. Dr. Merrill was the executive chairman of the Power Industry Computer Applications (PICA) Policy Committee for four years, and is currently a fellow of IEEE. He is the author of more than 70 technical publications on the power industry. Dr. Merrill holds an undergraduate degree in mathematics from the University of Utah and a Ph.D. in electrical engineering from MIT.

TIMOTHY DOUGLAS MOUNT is professor at Cornell University in the Department of Applied Economics and Management. His research areas include market power and price volatility in restructured markets for electricity, alternative auction institutions for electric power markets, as well as global environmental economics. Among other societies, he is a member of the International Association of Energy Economics, American Statistical Association, and Association of Environmental and Resource Economists. Professor Mount has published numerous articles on the power industry as well as environmental and agricultural economics. He received his doctorate in agricultural economics from the University of California at Berkeley.

SHMUEL S. OREN is Professor of Industrial Engineering and Operations Research at the University of California at Berkeley. With a doctoral degree from Stanford University in Engineering Economic Systems, Dr. Oren's research has focused on electric power system economics, and in particular on optimization and pricing strategies. In addition to his position at Berkeley, Dr. Oren has served as an expert consultant to numerous agencies, research institutes, and private entities including EPRI, SRI International, Niagara Mohawk Power Corporation, Entergy, and the Texas Public Utility Commission. He is a Senior Member of IEEE's Power Engineering Systems Society, as well as a member of the Institute for Operations Research and Management Science (INFORMS), the International Association of Energy Economists (IAEE), and the Mathematical Programming Society. Dr. Oren serves on the editorial boards of both INTERFACES and ENERGY ECONOMICS, and has published dozens of professional articles in his field, covering such topics as transmission congestion, flow-based transmission rights, generation unit commitment methods, and market pricing methodologies.

MICHAEL H. ROTHKOPF received his doctorate in operations research from MIT in 1964, and has been a professor of management and operations research at Rutgers University since 1988. He has served as the senior scientist as Lawrence Berkeley Laboratory, as well as leading their energy analysis program. His research and professional interests of long standing include models of markets and of competitive bidding, applications of operation research, and energy economics. Professor Rothkopf has edited a book on the power generation-unit commitment problem. In addition, he has written over 50 papers that have appeared in archival journals. Professor Rothkopf is a member of the Institute for Operations Research and Management Science, International Association of Energy Economists and American Economic Association. In addition, he was Editor-in-Chief of *Interfaces* from 1993 to 2000, and area editor for Operations Research Practice for the Journal Operations Research from 1984 to 1993. Professor Rothkopf is also a part-time consultant for FERC.

ROY J. SHANKER received his doctorate in industrial administration from Carnegie Mellon University in 1975. Dr. Shanker has been an independent consultant since 1981, providing management and economic consulting services in natural resource-related industries, particularly in the electric and natural gas utilities. In this capacity he currently serves on the Energy Markets Committee, the Transmission Expansion Advisory Committee and the Tariff Committee of the Pennsylvania Maryland and New Jersey (PJM) Office of Interconnection. Dr. Shanker also serves as a member of the New York Independent System Operator Technical Information Exchange Committee and participates on the NYISO Business Issues Committee, the Scheduling and Pricing Working Group, the Market Structure Working Group and several other working groups supporting the New York wholesale electric market.

THOMAS R. SCHNEIDER is a principal in the consulting firm of TRSenergy in Portola Valley, CA, specializing in technology evaluation and product positioning in restructured electricity markets, in addition to the development and implementation of technology acquisition strategy. From 1987 to 1997 Dr. Schneider was the executive scientist at the Electric Power Research Institute in Palo Alto, California, where he conceived and led institute efforts to sponsor fundamental and novel research in power systems engineering, as well as identifying the importance of power-industry restructuring on power system operations and reliability. In addition to numerous other appointments in the power industry, Dr. Schneider is currently the Chairman of the IEEE-USA Energy Policy Committee, where he served as Vice Chairman from 1998 to 2000, and a member of the IEEE Technology Policy Council. Dr. Schneider has contributed extensively to books on the power industry, proceedings and congressional testimony, and holds a Ph.D. in Physics from the University of Pennsylvania.

RICHARD TABORS is an engineering economist and scientist with over 30 years of domestic and international experience in energy systems planning and pricing. Dr. Tabors is President and founder of Tabors, Caramanis and Associates (TCA), an engineering and economics consulting firm specializing in policy development, business planning and technical analysis in the energy and utility sectors in the United States and internationally. He is also Senior Lecturer in Technology and Policy at Massachusetts Institute of Technology and has provided testimony and worked with clients throughout the country. His work with coauthors Fred C. Schweppe, Michael Caramanis and Roger Bohn published in SPOT PRICING OF ELECTRICITY is recognized as one of the theoretical foundations of electric industry pricing and restructuring. Dr. Tabors earned his undergraduate degree from Dartmouth College, and his doctorate from the Maxwell School at Syracuse University. He

is co-author of 5 books and over 100 professional articles and reports. He is a member of the IEEE and the International Association of Energy Economists.

ROBERT J. THOMAS is Professor of Electrical Engineering at Cornell University, where he specializes in power systems analysis and in particular the analysis and control of linear and nonlinear continuous and discrete time dynamical systems, complex networks, and applications of these to large-scale electric power systems. He is also currently the Director of the Power Systems Engineering Research Center (PSERC), a National Science Foundation Center and a Steering Committee Member for the Consortium for Electric Reliability Technology Solutions (CERTS). Dr. Thomas' affiliations and awards are far too numerous to list in full, but have included a variety of memberships and positions with the USDOE Secretary of Energy's Power Outage Study Team, the Institute for Research and Education for Electric Power, the Edison Electric Institute, and Drexel University's Department of Electrical and Computer Engineering Advisory Committee. He is a member of the Board of the IEEE and Chair of the IEEE Technology Policy Council. He has published approximately 60 professional articles and served as Editor for a number of prestigious technical journals. Dr. Thomas received his undergraduate, masters, and doctoral degrees in Electrical Engineering from Wayne State University.

LEE WILLIS is a registered professional electrical engineer with 30 years of experience in the electric power industry, specializing in transmission and distribution systems issues. Currently Vice President of Technology and Strategy at ABB Consulting, he has held executive positions with ABB Inc as Vice President of Distribution Systems, Director of Technology for Distribution Automation, and as an Institute Fellow at ABB's R&D Lab. He has also held positions in transmission and distribution at Westinghouse Electric and Houston Lighting and

Power. He is a Fellow of the IEEE, a member of the National Research Council, and the editor of the Power Engineering Series for Marcel Dekker Publishers of New York. He is the author or coauthor of 47 engineering journal articles, and five books including the POWER DISTRIBUTION PLANNING REFERENCE BOOK, SPACIAL ELECTRIC LOAD FORECASTING, and DISTRIBUTED POWER GENERATION–PLANNING AND EVALUATION. He earned his undergraduate and master's degrees in electrical engineering from Rice University.

BRUCE F. WOLLENBERG has been a professor in the Electrical Engineering Department at the University of Minnesota, Twin Cities, since 1989. Prior to his appointment, he worked at Control Data Corporation's Energy Management System Division, where he was responsible for the development of Artificial Systems Applications. He consulted on advanced research projects in energy management system application software, and he also participated in the power system operator training simulator project for the Electric Power Research Institute. Professor Wollenberg's current interests involve the development of large scale network solution algorithms using vector processing supercomputers, the extension of traditional power system control techniques to incorporate spot pricing algorithms and distributed computer technologies, as well as the application of expert systems to enhance the information presented to power system operators using real time computers.

MAY 31 2001 (13) (13)

Nos. 00-568 and 00-809

MOTION FILED

MAY 3 1 2001

IN THE

Supreme Court of the United States

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

---

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND BRIEF FOR THE PENNSYLVANIA PUBLIC UTILITY COMMISSION AS *AMICUS CURIAE* SUPPORTING RESPONDENTS

BOHDAN R. PANKIW
Chief Counsel
KAREN O. MOURY
Deputy Chief Counsel
JOHN A. LEVIN *
Assistant Counsel
PENNSYLVANIA PUBLIC UTILITY COMMISSION
Post Office Box 3265
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17105-3265
(717) 787-5978

* Counsel of Record

Counsel for Amicus Curiae the Pennsylvania Public Utility Commission

BEST AVAILABLE COPY

– WASHINGTON, D. C. 20001

26 pp

IN THE

Supreme Court of the United States

Nos. 00-568 and 00-809

PEOPLE OF THE STATE OF NEW YORK AND THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

ENRON POWER MARKETING, INC.,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE*

The Pennsylvania Public Utility Commission (Commission) hereby respectfully moves for leave to file the attached brief *amicus curiae* in this case, having failed to secure the consent of all parties.

There are a large number of parties in this case. The consent of all parties was sought by letter dated May 17, 2001 forwarded to each party on the Court's official docket list by overnight courier or United States Express Mail.

As of the date of the printing of this brief, 58 parties have consented and none have refused consent. Four requests were returned as undeliverable and 65 parties have not responded to our request as of the printing date of this brief.

The interest of the Commission in this proceeding is as a State agency which, pursuant to State legislation, has restructured its electric industry for the purpose of introducing retail competition, and which views the Federal Energy Regulatory Commission Order under attack as vital to the success of retail competition and the economic health of the Mid-Atlantic region. The Commission's views are not adequately represented by petitioners, respondents or other parties. It is believed that the views contained herein will provide more complete view of the Constitutional and statutory issues involved.

Respectfully submitted,

BOHDAN R. PANKIW
Chief Counsel
KAREN O. MOURY
Deputy Chief Counsel
JOHN A. LEVIN *
Assistant Counsel
PENNSYLVANIA PUBLIC UTILITY COMMISSION
Post Office Box 3265
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17105-3265
(717) 787-5978

* Counsel of Record

Counsel for Amicus Curiae the Pennsylvania Public Utility Commission

QUESTION PRESENTED IN NO. 00-568

Whether, given that Congress in 1935 stated that federal regulation extends "only to those matters which are not subject to regulation by the states" (Section 201(a) of Federal Power Act), and transmission of energy from generators to retail customers in the same State was then "subject to regulation by states" (as it has been since 1935), may FERC preempt State jurisdiction over such intrastate retail transmissions of electric energy?

QUESTIONS PRESENTED IN NO. 00-809

Whether the Federal Energy Regulatory Commission (FERC) has jurisdiction under the Federal Power Act (FPA), 16 U.S.C. §§ 798 *et seq.*, to regulate all transmission of electric energy in interstate commerce, including interstate transmission of electric energy that is sold to retail customers at a "bundled" price?

Whether FERC had jurisdiction and the obligation under the FPA to eliminate pervasive "undue discrimination" in the provision of interstate electric energy transmission services by requiring transmission-owning utilities to provide interstate transmission services on the same terms to all users, for all interstate transmissions, including transmissions bundled with retail sales?

Whether the court of appeals erred in ruling that FERC had discretion to interpret the FPA as denying FERC the necessary jurisdiction to remedy the undue discrimination it had found in the provision of interstate transmission?

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	iv
STATEMENT OF *AMICUS* INTEREST	1
SUMMARY OF ARGUMENT	2
ARGUMENT	4
I. ORDER 888 AND THE EXERCISE OF STATUTORY AND FEDERAL COMMERCE CLAUSE AUTHORITY BY FERC IS SUPPORTED BOTH BY LAW AND BY CHANGES IN THE NATIONAL TRANSMISSION SYSTEM	4
A. The Legislative History of The Federal Power Act and the Energy Policy Act of 1992 Demonstrates That Congress Intends to Create a Vibrant Wholesale Generation Market	4
B. The Development of Pennsylvania Retail Competition Is Based Upon A Vibrant Wholesale Generation Market and An Interstate Grid Not Controlled by Parochial Local Interests	9
C. Parochial State Rules Which Burden the Operation of the Interstate Transmission Network Burden Interstate Commerce Present Obstacles To Congress's Plan For Wholesale Competition and Endanger the Reliability of the Interstate Transmission Network	12
CONCLUSION	17

TABLE OF AUTHORITIES

CASES: Page

Duquesne Light and Penn Power v. Barasch, 488 U.S. 299 (1989) 7-8

Northern States Power v. Federal Energy Regulatory Commission, 176 F.3d 1090 (CA 8th Cir. 1999), *cert. den sub nom. Enron Power Marketing Inc. v. Northern States Power Co.*, 528 U.S. 1182 (2000) 8-9

Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) 4

Pennsylvania Water & Power Co. v. Federal Power Commission, 343 U.S. 414 at 420 (1952) 5

Rhode Island PUC v. Attleboro Steam, 273 U.S. 83 (1927) 2

United States v. Public Utilities Commission of California, 345 U.S. 295 (1952) 5

CONSTITUTIONAL PROVISIONS:

Commerce Clause. U.S. Const. Art. 1, § 8, cl. 3. .. 2

STATUTES:

Federal Statutes:

15 U.S.C. § 32 6
16 U.S.C. §§ 792 *et seq* 2
16 U.S.C. § 824a 5
16 U.S.C. § 824j 5
16 U.S.C. § 824j (b) 14
16 U.S.C. §§ 824j-824m 2
16 U.S.C. § 824k 14
16 U.S.C. § 824k (h) 6

TABLE OF AUTHORITIES—Continued

Page

State Statutes:

66 Pa. C.S. § 101, *et seq.* 1, 9-10
66 Pa. C.S. § 2801–2812 1
66 Pa. C.S. § 2802 (1), (3), (5), (13), (15), (19) and (20) 10
66 Pa. C.S. § 2802 (12) 10
66 Pa. C.S. § 2803 10

ADMINISTRATIVE CASES:

Allegheny Power System on behalf of Monongahela Power Company, The Potomac Edison Company, West Penn Power Company, PJM Interconnection, L.L.C., Allegheny Power Service Corporation, 95 F.E.R.C. ¶61,045 (2001) 12

City of Vernon, California v. California Independent System Operator, F.E.R.C. Docket No. EL01-75-000 (Complaint filed May 7, 2001) 13-14

Duquesne Light Co., F.E.R.C. Docket No. RT01-13-000, *Status Report of Duquesne Light Company*, (December 5, 2000) 12

Electric Utility Restructuring Filings Made Pursuant to 66 Pa.C.S. § 2806(E), 176 PUR 4th 45 (Pa.P.U.C. 1997) 10

North American Electric Reliability Council, 85 F.E.R.C. ¶ 61,353 (1998) 15

Order Approving PJM Supporting Companies' Request for Market-Based Pricing Authority, 86 F.E.R.C. ¶61,248 (1999). 11

Pennsylvania Water & Power Co., 8 F.P.C. 1, 37 (1949) 5

TABLE OF AUTHORITIES—Continued

Page

Pennsylvania - New Jersey - Maryland Interconnection, 81 F.E.R.C. ¶ 61,257 (1997), *order on clarification*, 82 F.E.R.C. ¶ 61,068 (1998), *order on reh'g*, 92 F.E.R.C. ¶ 61,782 (2000), *appealed sub nom Baltimore Gas and Electric Co. v. F.E.R.C.*, Case No. 00-1460 (CA District of Columbia) and *Public Service Electric and Gas Company v. F.E.R.C.*, Case No. 00-1457 (CA District of Columbia). 11

Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, F.E.R.C. Stats. & Regs. ¶31,036 (1996), *order on reh'g, Order No. 888-A*, F.E.R.C. Stats. & Regs. ¶ 31,048 (1997), *order on reh'g, Order No. 888-B*, 81 F.E.R.C. ¶61,248 (1997), *order on reh'g, Order No. 888-C*, 82 F.E.R.C. ¶61,046 (1998), *aff'd in part and remanded in part sub nom. Transmission Access Policy Study Group, et al. v. F.E.R.C.*, 225 F.3d 667 (D.C. Cir. 2000), *pet. for cert granted sub nom. People of the State of New York v. F.E.R.C.*, No. 00-568 and *Enron Power Marketing, Inc. v. F.E.R.C.* (Order No. 888),—U.S.—, 149 L. Ed. 102, 121 S. Ct. 1185 (U.S. 2001) (*Order 888*). ..... *passim*

LEGISLATIVE MATERIALS:

H. R. 5423, 74th Cong., 1st Sess.; S. 1725, 74th Cong., 1st Sess 5

S. Rep. No. 621, 74th Cong., 1st Sess., 19 5

TABLE OF AUTHORITIES—Continued

Page

Evolving Federal and State Roles, Hearings before the House Subcommittee on Energy and Power, 106th Congress at 91 (March 18, 1999) 3

Electricity Markets, Hearings before the House Subcommittee on Energy and Air Quality, 107th Congress (February 15, 2001)..... 3

OTHER MATERIALS:

William H. Penniman and Paul B. Turner, *A Jurisdictional Clash over Electricity Transmission: Northern States Power v. F.E.R.C.*, 20 Energy L. J. 205 (1999)..... 9

STATEMENT OF *AMICUS* INTEREST [1]

The Pennsylvania Public Utility Commission is a State administrative commission created by the General Assembly of the Commonwealth of Pennsylvania and is charged with the regulation of electric utilities and licensing of generation suppliers within the Commonwealth of Pennsylvania. 66 Pa.C.S. § 101, *et seq*. The Commonwealth of Pennsylvania continues to be involved in the restructuring of the Commonwealth's retail electric energy industry pursuant to the Commonwealth's *Electricity Generation Customer Choice and Competition Act*, 66 Pa.C.S. § 2801-2812 ("Pennsylvania Electric Competition Act"). Since January 2, 2000, nearly all retail electric customers in the Commonwealth have had the right to select a competitive retail electric generation supplier according to the terms of the Pennsylvania Electric Competition Act. As the success of the retail electric market is dependent upon a well-functioning regional wholesale generation market, the Commission urges this Court to sustain the orders below. FERC's conclusion that the Federal Power Act requires interstate transmission service to be provided on the same terms and conditions for all is in accord with law and Congressional intent. The Pennsylvania Commission supports FERC's orders[2] carrying

---

[1] Rule 37.6 Statement: John A. Levin, Assistant Counsel to the Pennsylvania Public Utility Commission, is the author of this brief. No person or entity other than the Pennsylvania Public Utility Commission has made a monetary contribution to the preparation or submission of this brief.

[2] *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888*, F.E.R.C. Stats. & Regs. ¶31,036 (1996), *order on reh'g, Order No. 888-A*, F.E.R.C. Stats. & Regs. ¶ 31,048 (1997), *order on reh'g, Order No. 888-B*, 81 F.E.R.C. ¶61,248 (1997), *order on reh'g, Order No. 888-C*, 82 F.E.R.C. ¶61,046 (1998), *aff'd in part and remanded in part sub nom. Transmission Access Policy Study Group, et al. v. F.E.R.C.*, 225 F.3d 667

out the intent of Congress's enactment of the Energy Policy Act of 1992. FERC's jurisdiction over the provision of interstate transmission service under the Federal Power Act does not change whether the power to be transmitted is carried to a State which permits retail electric competition or to a State which continues to regulate bundled retail service in traditional fashion. A State may not, under the guise of local regulation, place an undue burden upon interstate commerce and the interstate transmission system.

SUMMARY OF ARGUMENT

This Court determined, in *Rhode Island PUC v. Attleboro Steam*, 273 U.S. 83 (1927) that interstate electric transmission service could not lawfully be regulated by the States based upon repugnance of such regulation to the Commerce Clause. U.S. Const. Art. 1, § 8, cl. 3. In the intervening years, it became apparent to Congress that there was an important regulatory gap created by the unregulated growth of the electric system across State lines, accompanied by changes in technology. Congress's response was to fill the regulatory gap eight years later by passage of the Federal Power Act of 1935, 16 U.S.C. §§ 792 *et seq.*. Through the Federal Power Act, the federal government assumed jurisdiction over the rates, rules and regulations of bulk power sales and interstate transmission, while the States regulated the provision of intrastate transmission service then associated with the bundled retail sales of electricity to end users. This regulatory paradigm remained more or less static until 1992.

In 1992, Congress passed the Energy Policy Act of 1992 (EPAct), containing provisions codified at 16 U.S.C. §§ 824j-824m introducing open access to the transmission grid and

(D.C. Cir. 2000), *pet. for cert granted sub nom. People of the State of New York v. F.E.R.C.*, No. 00-568 and *Enron Power Marketing, Inc. v. F.E.R.C.* (Order No. 888), __ U.S. __, 149 L. Ed. 102, 121 S. Ct. 1185 (U.S. 2001) (*Order 888*).

competition to wholesale generation markets. The creation of wholesale competition provided the necessary predicate to retail competition. Orders 888, challenged here by both Petitioners New York and Enron, was FERC's comprehensive implementation of the regulatory changes wrought by EPAct.

As a State that has been among the leaders in the introduction of retail electric competition[3], Pennsylvania has an important stake in the wholesale generation market protections created by FERC Orders 888 and 889. An interstate transmission system riddled with "holes" or "blockades" created by the erection of local State rules seeking to protect "native" bundled retail load would be injurious to interstate commerce, retail competition, regional reliability and at odds with Congressional intent.

The electric transmission grid of 1928 or 1935 or 1992 is not the electric transmission grid of today. Industries can and do grow from localized markets with little effect on interstate commerce to national markets spanning many or all states. Wholesale generation markets are becoming increasingly regional and multi-state in character. FERC's reorganization of transmission under "Open Access Transmission Tariffs" and the control of Independent System Operators and

[3] Of 1.2 million customers eligible to shop for competitive retail power in Pennsylvania in March, 1999, 400,000 had actually switched, about 33 percent of peak winter load. Testimony of John M. Quain, Chairman, Pennsylvania Public Utility Commission, *Evolving Federal and State Roles, Hearings before the House Subcommittee on Energy and Power*, 106th Congress at 91 (March 18, 1999) As of October 2000, more than 550,000 Pennsylvania customers were purchasing power from a competitive supplier. In 1997, retail rates were on average 15% higher than elsewhere in the United States. In February, 2001, Pennsylvania rates were 4.4% lower on average. Testimony of John M. Quain, Chairman, Pennsylvania Public Utility Commission, *Electricity Markets, Hearings before the House Subcommittee on Energy and Air Quality*, 107th Congress at 91 (February 15, 2001)

Regional Transmission Organizations are both a reflection and a necessary facilitator of this trend. Regional markets cannot effectively operate where individual states are permitted to carve out portions of the common grid in promotion of local policies or local industries. Congress cannot be presumed to have opened up the transmission grid to competition through the enactment of EPAct, only to see its policy chopped apart by individual States or the political subdivisions of States seeking to advance local parochial interests under the guise of the exercise of "traditional police powers".

ARGUMENT

I. ORDER 888 AND THE EXERCISE OF STATUTORY AND FEDERAL COMMERCE CLAUSE AUTHORITY BY FERC IS SUPPORTED BOTH BY LAW AND BY CHANGES IN THE NATIONAL TRANSMISSION SYSTEM

A. The Legislative History of The Federal Power Act and the Energy Policy Act of 1992 Demonstrates That Congress Intends to Create a Vibrant Wholesale Generation Market

Transmission facilities, prior to EPAct, were universally operated by and for the benefit of the vertically integrated monopoly owners of such facilities. The provisions of the Federal Power Act were crafted by Congress to encourage voluntary, not mandatory, interconnections of transmission networks. *Otter Tail Power Co. v. United States,* 410 U.S. 366 (1973). As this Court noted in *Otter Tail:*

> As originally conceived, Part II would have included a "common carrier" provision making it "the duty of every public utility to . . . transmit energy for any person upon reasonable request . . ." In addition, it would have empowered the Federal Power Commission to order wheeling if it found such action to be "necessary or desirable in the public interest." H. R. 5423, 74th Cong., 1st Sess.; S. 1725, 74th Cong., 1st Sess. These provisions were eliminated to preserve "the voluntary action of the utilities." S. Rep. No. 621, 74th Cong., 1st Sess., 19. It is clear, then, that Congress rejected a pervasive regulatory scheme for controlling the interstate distribution of power in favor of voluntary commercial relationships.

Otter Tail, at 374.

Although the then-existing provisions of Section 202 of the Federal Power Act, 16 U.S.C. § 824a, authorized FERC's predecessor, the Federal Power Commission (FPC), after hearing, to order interconnections between transmission facilities, this provision was generally interpreted as authority to require interconnections between utilities, not as authority to force utilities to act as common carriers.

Even so, this Court found it within the FPC's powers in 1952 to compel a Pennsylvania electric utility to continue its existing interconnection arrangement with a Maryland utility for the benefit of Maryland retail consumers, even "notwithstanding the fact that system energy transactions at some particular times may involve energy never crossing the State boundary." *Pennsylvania Water & Power Co. v. F.P.C.,* 343 U.S. 414 at 420 (1952), *citing, Pennsylvania Water & Power Co.,* 8 F.P.C. 1, 37 (1949). It should be noted that while *U.S. v. Public Utilities Commission of California,* 345 U.S. 295 (1952) usefully summarizes the intent of Congress with regard to the Federal / State jurisdictional issues prior to 1952, it and similar federal/state jurisdictional cases no longer control this case because of the enactment of EPAct in 1992.

EPAct signalled the intent of Congress that a sharp departure was to be made in the method and scope of regulation of the interstate transmission grid. The language of Title VII, Section 721 of EPAct, 16 U.S.C. § 824j, was a revolution in electric transmission regulation. For the first

time since the start of the electric power industry, any person could request transmission service to convey power from one point to another point for resale. This statutory provision was the launch by Congress of a wholesale electric generation market in the United States which implicitly encouraged, but did not require a parallel development by the States of a competitive retail generation market. It is indeed difficult to conceptualize any development of electric retail competition without a preexisting wholesale generation market. By permitting non-utility generation providers access to the grid, Congress was also encouraging an end to the traditional vertically integrated electric utility monopoly that had been the unchallenged United States model for most of the 20th century.

EPAct Title VII contained other important provisions. Section 711 of EPAct amended the Public Utility Holding Company Act of 1935 (PUHCA), 15 U.S.C. § 32, to create a new purely wholesale generation entity, the "exempt wholesale generator" which, subject to FERC review, would be exempt from the regulatory provisions of PUHCA. Thus Congress created a new kind of market participant for the new competitive wholesale generation market—exempt wholesale generators, free of geographic restrictions and monopoly utility control that would compete with incumbent monopoly generation and bring about market based prices and market reform.

The provision upon which New York principally relies, EPAct § 722, amends Section § 212 of the Federal Power Act by the addition of subsections (g)-(k), specifically subsection (h) "Prohibition on Mandatory Retail Wheeling and Sham Wholesale Transactions", 16 U.S.C. § 824k (h). The context of this subsection indicates Congress's overarching intent to create a wholesale generation market in interstate transmission of electricity while giving States flexibility to create retail electric competition or not, as each State

determined to be its policy. If States wish to introduce retail competition, EPAct creates the required wholesale generation market infrastructure. If not, States cannot be forced, through a Section 212 interconnection order to open up their retail markets to competition.

Congress never intended to and did not grant States the power to defeat Congress's creation of a wholesale transmission market by interposing parochial State burdens on the portions of the transmission grid which happened to be located in that State. While reserving to the States their preexisting power to regulate jurisdictional monopoly retail electric utility service as States had for most of the 20th Century, Congress did not intent to cede any of its jurisdiction over interstate transmission. Congress had no intent to impair the national wholesale electric generation market which it had created with the same stroke of the pen.

New York's *Brief on the Merits* erroneously conflates State ratemaking powers with rules controlling the operation of the interstate transmission network. Transmission rates are actually a relatively small component of retail electric rates. It is clear from New York's argument (and even more so from the novel theory advanced by California as *amicus curiae)* that retail rates are not the issue here. Network control and "rules of the road" are what is being fought over. Who controls the interstate grid gets to decide a great many things, including wholesale generation market design and which wholesale electricity transactions will flow and which will be cut or reduced.

Thus, New York's position that the matter before you is really a rate case and its citation of *Duquesne Light and Penn Power v. Barasch*, 488 U.S. 299 (1989) in support of that proposition is ironic in two respects.

First it is a *non sequitur*. The issues in this case clearly do not involve public utility rates or a claim that FERC has engaged in an unconstitutional "taking" of utility property, a

claim which New York would lack standing to advance in any event. In *Duquesne*, two Pennsylvania utilities challenged a Pennsylvania ratemaking statute involving State laws governing the valuation of *intra*state generation assets for State ratemaking purposes. Second, as this Court recognized in *Duquesne*, when utility regulatory schemes change, states must fairly adjust their rules and methods of regulation to accommodate such changes.

> The risks a utility faces are in large part defined by the rate methodology because utilities are virtually always public monopolies dealing in an essential service, and so relatively immune to the usual market risks. Consequently, a State's decision to arbitrarily switch back and forth between methodologies in a way which required investors to bear the risk of bad investments at some times while denying them the benefit of good investments at others would raise serious constitutional questions. But the instant case does not present this question.

Duquesne at 315.

Here, "methodologies" have clearly changed, at Congress's behest. New methodologies of participation and cooperation are necessary, both on FERC's behalf and on behalf of the States to ensure that the growing wholesale generation market in electricity generation is not hampered or destroyed by fragmentation of jurisdiction over the transmission grid.

In its *Brief for Respondents* in No. 00-809 New York cites to the decision of the Eighth Circuit in *Northern States Power v. F.E.R.C.*, 176 F.3d 1090 (CA 8th Cir. 1999), *cert. den sub nom. Enron Power Marketing Inc. v. Northern States Power Co.*, 528 U.S. 1182 (2000) for the principle that Congress intended that a State has jurisdiction to protect its "native load" customers by ordering that they receive preferential transmission service, whether or not that burdened interstate commerce. That decision is manifestly erroneous and this

Court should expressly overrule it. *See* William H. Penniman and Paul B. Turner, *A Jurisdictional Clash over Electricity Transmission: Northern States Power v. F.E.R.C.*, 20 Energy L. J. 205 (1999).

B. The Development of Pennsylvania Retail Competition Is Based Upon A Vibrant Wholesale Generation Market and An Interstate Grid Not Controlled by Parochial Local Interests

Prior to 1997, and the start of retail competition in the Commonwealth of Pennsylvania, the Pennsylvania Commission shared many of the views on jurisdiction presently being advanced by New York. The Pennsylvania Commission participated in the rulemaking proceedings that led to the issuance of Order 888, and in our May 23, 1996 petition for rehearing, the Pennsylvania Commission told FERC that it lacked jurisdiction to redefine its jurisdiction over interstate transmission in the manner that it ultimately did. At that time, none of the States had any actual experience with retail competition made possible by the existence of a nascent wholesale generation market. Pennsylvania's extensive and actual experience with the operation of competitive wholesale and retail generation markets has been the basis of a major evolution of our perspective.

The Pennsylvania Electric Competition Act was signed into law on December 3, 1996 and became effective January 1, 1997, contemporaneously with the development of the open access rules being developed in FERC's *Order 888* proceeding. The concepts and mechanisms being advanced by FERC in its *Order 888* rulemaking, particularly those provisions that sought to create a national wholesale generation market and transmission system free of undue discrimination or market power, played a central role in the development and eventual passage of the Pennsylvania Electric Competition Act.

The Pennsylvania Electric Competition Act was drafted contemporaneously with FERC's restructuring of the national wholesale generation markets through its Order 888 rulemaking and reflects FERC's restructuring efforts. For example, Pennsylvania legislative findings at 66 Pa.C.S. §2802 (1), (3), (5), (13), (15), (19) and (20) note recent changes in Federal law and policy which restructured previously regulated industries to competitive markets. 66 Pa.C.S. § 2802 (19) encourages all market participants to coordinate plans and transactions through a [FERC approved] independent system operator or functional equivalent.

66 Pa.C.S. § 2803 defines "direct access" as "the right of electric generation suppliers and end-use customers to utilize and interconnect with the electric transmission and distribution system on a nondiscriminatory basis at rates, terms and conditions of service comparable to the transmission and distribution companies' own use of the system to transport electricity from any generator of electricity to any end-use customer", a standard comparable to FERC's "open access" standard in Order 888. All of these provisions reflect Pennsylvania's reliance on the Federal restructuring rules embodied in *Order 888*.

The Pennsylvania Commission, assigned by the Pennsylvania General Assembly the task of implementing the Pennsylvania Competition Act, relied heavily upon the interstate transmission and wholesale generation market restructuring process that FERC has undertaken in *Order 888*, particularly with respect to FERC's guarantee of open access to the regional transmission grid to all wholesale generation market participants. *Electric Utility Restructuring Filings Made Pursuant to 66 Pa.C.S. § 2806(E)*, 176 PUR 4th 45 (Pa.P.U.C. 1997). A major concern of Pennsylvania was that "Electric industry restructuring should ensure the reliability of the interconnected electric system by maintaining the efficiency of the transmission and distribution system." *Id.* at 49, *citing* 66 Pa. C.S. §2802 (12).

Most of Pennsylvania's transmission grid is under the operational control of one of the nation's first independent system operators, created by FERC pursuant to the "open access" principles of *Order 888*[4]. PJM Interconnection, L.L.C. (PJM) controls the transmission facilities of nine transmission owning companies in the States of Pennsylvania, New Jersey, Maryland, Delaware and the District of Columbia. PJM's Open Access Transmission Tariff, as approved by FERC, permits anyone in the PJM region, upon joining PJM and signing its agreements to transport electric energy for resale over PJM controlled transmission facilities and pay a single networked tariff.

Market based wholesale generation pricing authority has been granted by FERC to numerous participants in the PJM region, including generation owners which also own or control transmission facilities. Such market pricing authority has been granted expressly *because* market power concerns have been adequately addressed by PJM's independent control of the region's transmission facilities. *Order Approving PJM Supporting Companies' Request for Market-Based Pricing Authority*, 86 F.E.R.C. ¶ 61,248 (1999). Absent transmission system control by an independent entity, FERC correctly concludes that a transmission owner that also participates in the wholesale generation market has great incentive and opportunity to disadvantage generation competitors without such control.

The PJM ISO control area is expanding, increasing the size of the Mid-Atlantic regional market for wholesale electricity. The Allegheny Power System, which serves portions of

---

[4] *Pennsylvania - New Jersey - Maryland Interconnection*, 81 F.E.R.C. ¶ 61,257 (1997), *order on clarification*, 82 F.E.R.C. ¶ 61,068 (1998), *order on reh'g*, 92 F.E.R.C. ¶ 61,782 (2000), *appealed sub nom Baltimore Gas and Electric Co. v. F.E.R.C.*, Case No. 00-1460 (CA District of Columbia) and *Public Service Electric and Gas Company v. F.E.R.C.*, Case No. 00-1457 (CA District of Columbia).

western Pennsylvania, Maryland, Ohio, Virginia and West Virginia has already announced plans to join PJM. *Allegheny Power System on behalf of Monongahela Power Company, The Potomac Edison Company, West Penn Power Company, PJM Interconnection, L.L.C., Allegheny Power Service Corporation,* 95 F.E.R.C. ¶ 61,045 (2001). Duquesne Light Company has announced similar tentative plans to join PJM. *Duquesne Light Co.*, F.E.R.C. Docket No. RT01-13-000, *Status Report of Duquesne Light Company,* (December 5, 2000).

Thus, most of Pennsylvania is or will soon be served by an Independent System Operator which spans much of the Mid-Atlantic seacoast of the United States from New Jersey to Virginia, including the District of Columbia and seven States.

C. Parochial State Rules Which Burden the Operation of the Interstate Transmission Network Burden Interstate Commerce Present Obstacles To Congress's Plan For Wholesale Competition and Endanger the Reliability of the Interstate Transmission Network

New York's view is that any transaction, wholesale or retail, which begins and ends in a single State is wholly State jurisdictional regardless of its impact on the interstate transmission network. If that is true then there is no limit to a State's authority to give preference to such transactions over interstate commerce, even to the point of blocking such transactions entirely. "State" police powers are also exercised by political subdivisions of states, such as "utility districts" or municipal light and heating authorities. While such State political entities exercise "traditional police powers" they are also connected to the interstate grid. There is considerable scope for mischief in such a misreading of the Federal Power Act. A State or political subdivision located along a path of interstate transmission congestion or strategic importance

could, by preferential scheduling of power transactions, equipment outages or emergency operations, control a large portion of the interstate grid.

For example, PJM members are signatories to a number of agreements, including an Operating Agreement and a Reliability Agreement, which obligate PJM wholesale generation market participants, transmission owners, generation owners and local distribution companies to coordinate system operations, system outages, voltage reductions and load dumps in times of serious shortages. Such coordinated control and response is essential to transmission system security. Under New York's theory, any State (or political subdivision with transmission resources or control) could substitute its own judgment during a regional, multi-state emergency.

There is nothing hypothetical or speculative about such concerns. The City of Vernon, California filed a recent complaint with FERC asking it to relieve the City of the obligation to interrupt during times of California transmission system emergency declared by the California ISO. *City of Vernon, California v. California Independent System Operator,* F.E.R.C. Docket No. EL01- 75-000 (Complaint filed May 7, 2001). In its complaint, the City declares:

> It is widely reported that California is likely to suffer shortages of power supply this summer. Some projections are that as a result of such shortages blackouts will be required for 30 days or more. In the past, when the ISO system, or a portion of that system, was short of energy in real time, the ISO has imposed rotating blackouts that required all utilities to blackout a portion of their load on a pro rata basis with other utilities on the ISO system generally or on the particular affected portion of the system. Whether the particular utility was fully resourced or fully scheduled or not, was not taken into account . . . [T]he ISO's response to Vernon is that the failure or inability of other utilities to schedule sufficient supplies for their load, and the ISO's inability

> to makeup the shortfall with real time imbalance energy, constitutes a "system emergency". The ISO contends that under its tariff and various agreements to which Vernon is a party, Vernon and all other utilities in the affected area must curtail their customers' load on the same pro rata basis in such system emergencies . . .
>
> However, the present circumstances are not "system emergencies" within that meaning. The present circumstances are the results of choices made by or for the utilities that find themselves short of supply. They are not the result of some sudden and unexpected calamity.

City of Vernon, California v. California Independent System Operator, F.E.R.C. Docket No. EL01-75-000 (Complaint filed May 7, 2001) at 3-9.

The prospect of a California municipality sitting as a lighted island while its neighbors struggle in the darkness to cope with a chronic system emergency is a vision of chaos. The City of Vernon's demand would impair California's and the Western Interconnection's efforts to battle a serious regional shortage of electricity and transmission capacity and spark disputes which could lead to the fragmentation of the regional transmission grid. Indeed, the City's complaint is a harbinger of the future of the interstate transmission grid as New York would have it controlled under a system of fragmented jurisdiction.

Whatever the ultimate resolution of the *City of Vernon* complaint, FERC must assess the complaint's effect on reliability, 16 U.S.C. §824j (b), and its impact on the interstate transmission system, 16 U.S.C. §824k. FERC is obligated under the Federal Power Act to protect the reliability and integrity of the larger interstate transmission system as a whole, so as to protect the national public interest.

New York would put itself in FERC's place in resolving such disputes. New York claims a unilateral and seemingly unconstrained power, free of FERC review or jurisdiction, to "protect" a certain class of New York retail customers by running those portions of the New York transmission system it deems "intrastate". It would do so by carving out superior rights to facilities that are part of the interstate transmission system, to the detriment of neighboring regions. While New York is understandably vague on the details of how it would exercise this asserted power, the harm to interstate commerce is clear. There will be two classes of firm transmission service in New York: "Bundled Retail Firm" and "Interstate Commerce Firm". Interstate commerce will be less firm than New York's bundled retail load and the degree of burden upon interstate commerce will be at New York's behest.

Pennsylvania and other states which depend upon a well functioning wholesale transmission system and competitive wholesale generation market cannot avoid being disadvantaged by such a claim. With wholesale transactions frequently spanning states and regions, every State through which any portion of a transaction might flow could assert jurisdiction to regulate or impede it. Indeed, as electric energy does not flow directly from one point to another, but over many parallel pathways in the interstate transmission grid, nearly every wholesale power transaction in the Eastern Interconnection could conceivably come under New York's jurisdiction. *See North American Electric Reliability Council,* 85 F.E.R.C. ¶ 61,353 (1998).

The development and operation of regional independent system operators such as PJM is threatened as well. Pennsylvania regards such regional transmission organizations, which operate regional transmission grids under common control and market rules, as essential to well functioning wholesale and retail markets. With regional wholesale generation markets gradually increasing in size, it

is important that the interstate grid be protected against efforts to carve it up into many individual State grids with many and differing State transmission rules.

As discussed above, Congress intended to leave States with their existing retail ratemaking role. However, Congress also intended to create a vibrant wholesale transmission market by removing the previous monopoly utility control of the grid which excluded willing wholesale buyers and sellers of electric generation capacity.

The assertion by a State of a right to carve out and control transmission facilities connected to the interstate grid for the benefit of certain of its citizens is inimical to law, public policy and Congressional intent. New York's position is thus inconsistent with the Interstate Commerce Clause, the Federal Power Act and the Energy Policy Act of 1992.

On the other hand, the assertion of Enron Power Marketing, Inc. (Enron) in its brief that FERC should be compelled to extend its Open Access Transmission Tariff requirements to open up bundled retail sales to FERC jurisdiction is not supported by the record below, and is contrary to the intent of Congress that traditional State rate regulation of bundled electric service be permitted to continue. Should FERC conclude that a particular State statute or rule has exceeded state jurisdictional bounds by burdening interstate commerce or by creating undue discrimination against other wholesale customers dependent on the interstate grid, FERC has ample power to remedy such burden by order or rule.

CONCLUSION

The judgment of the Court of Appeals for the District of Columbia should be affirmed.

Respectfully submitted,

BOHDAN R. PANKIW
Chief Counsel
KAREN O. MOURY
Deputy Chief Counsel
JOHN A. LEVIN *
Assistant Counsel
PENNSYLVANIA PUBLIC UTILITY COMMISSION
Post Office Box 3265
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17105-3265
(717) 787-5978

* Counsel of Record

Counsel for Amicus Curiae the Pennsylvania Public Utility Commission